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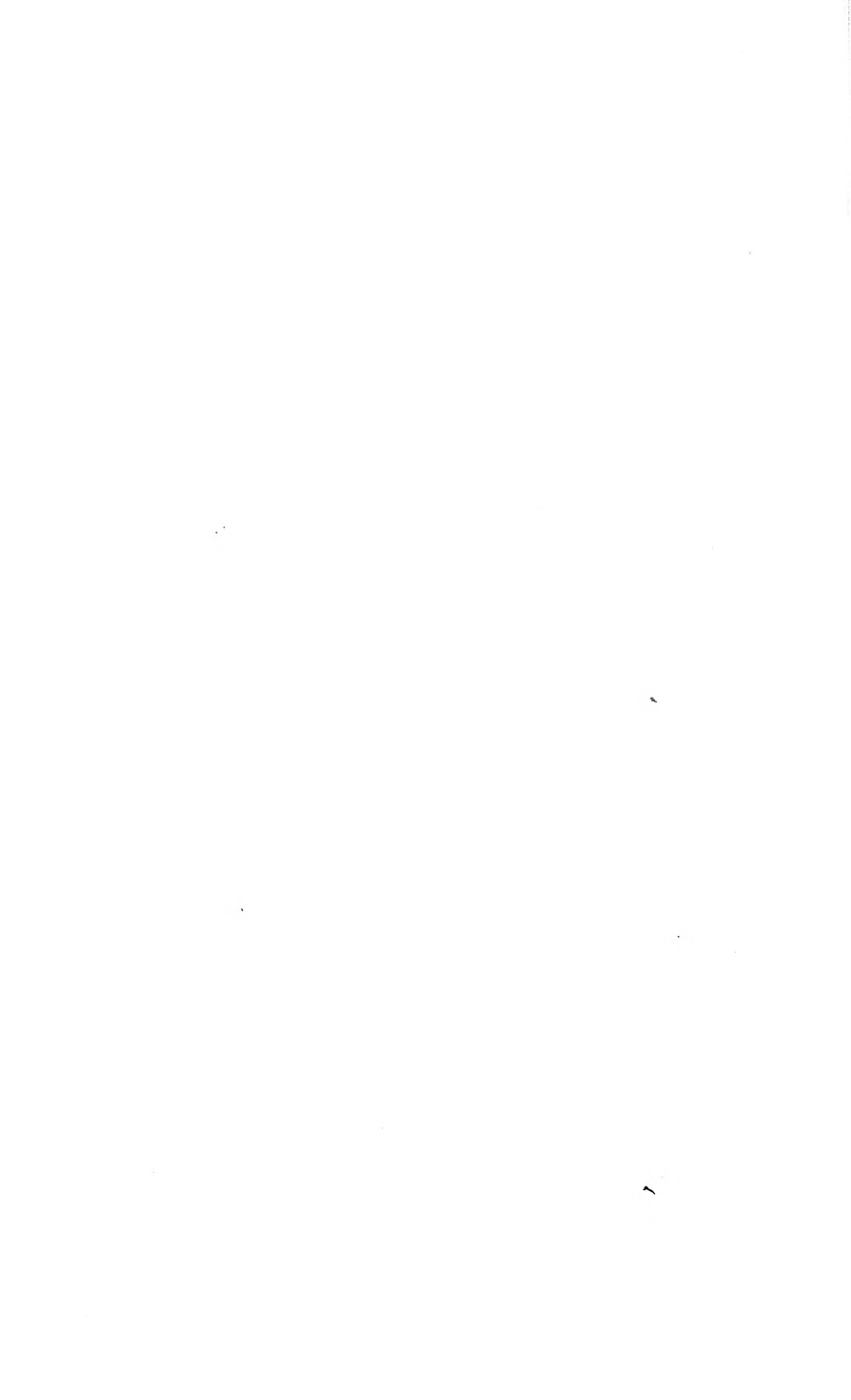
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2455
No. 11688

United States
Circuit Court of Appeals
For the Ninth Circuit

THOMAS H. BRODHEAD, doing business as
T. H. Brodhead Co.,

Appellant,

vs.

WILLIAM BORTHWICK, Tax Commissioner and
Tax Collector of the Territory of Hawaii,
Appellee.

Transcript of Record

Upon Appeal from the Supreme Court
for the Territory of Hawaii

FILED
SEP 19 1947

PAUL P. O'BRIEN, /

CLERK

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

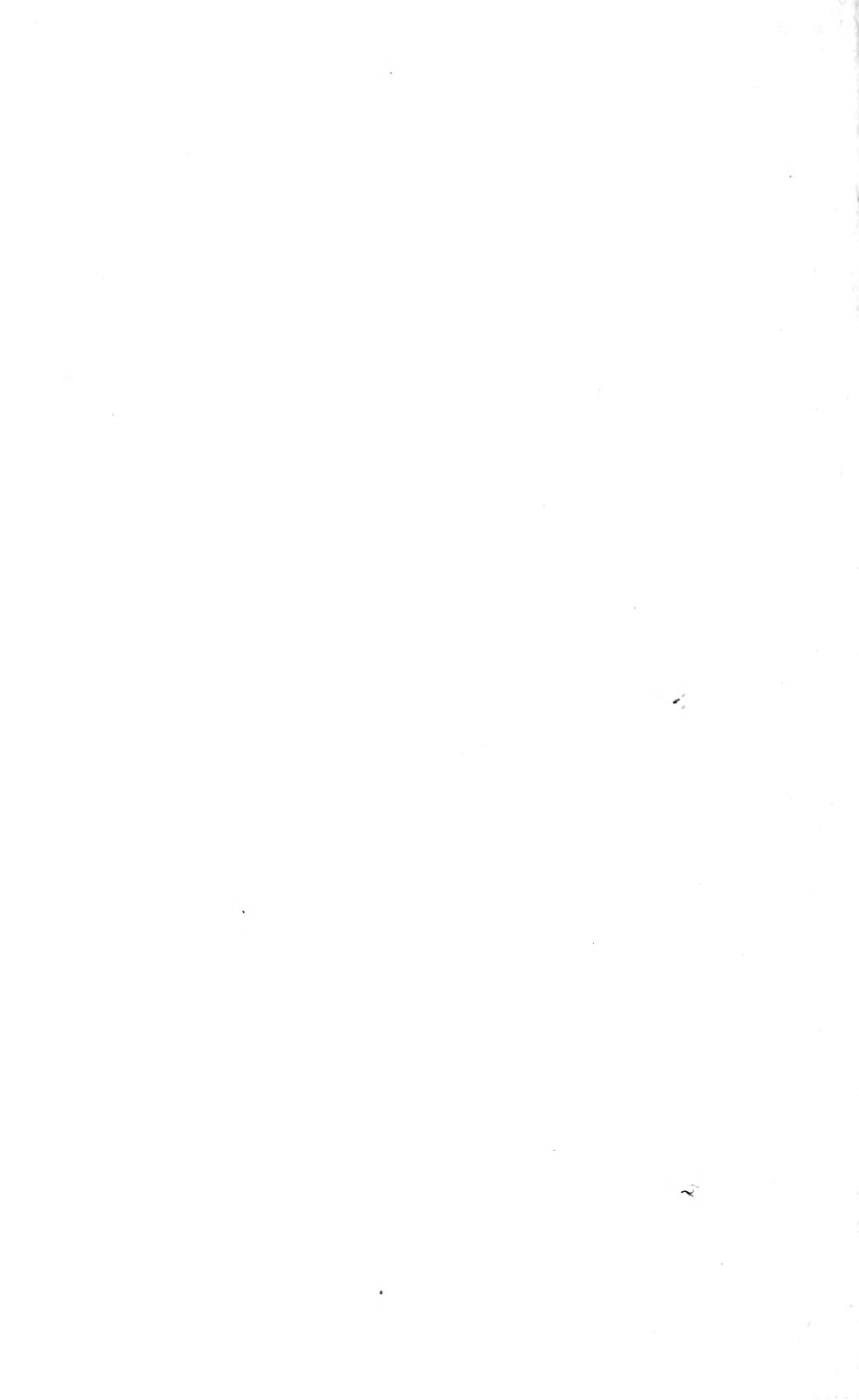
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* Page numbering appearing at foot of page of original certified Transcript of Record.

In the Circuit Court of the First Judicial Circuit
Territory of Hawaii

L. No. 17365

At Term In Law

THOMAS H. BRODHEAD, d.b.a
T. H. BRODHEAD CO.,

Plaintiff,

vs.

WILLIAM BORTHWICK, Tax Commissioner
and Tax Collector,

Defendant.

Action to Recover Gross Income Taxes
Paid Under Protest

COMPLAINT

To the Honorable, the Presiding Judge, at Term,
of the Circuit Court of the First Judicial Cir-
cuit, Territory of Hawaii:

Comes now Thomas H. Brodhead, doing business
as T. H. Brodhead Co., plaintiff above named, and
for cause of action against the defendant above
named, alleges as follows:

I.

That plaintiff is, and at all times hereinafter
mentioned was, a resident of Honolulu, City and
County of Honolulu, Territory of Hawaii; and that
the plaintiff above named is the general partner of
a registered special partnership, doing business in

Honolulu aforesaid under the firm name and style of T. H. Brodhead Co.

II.

That defendant above named is and was at all relevant times the duly appointed, qualified and acting Tax Commissioner of the Territory of Hawaii, and as such is and was at all relevant times in charge of the administration and enforcement of Act 141 (Series A-44) of the Session Laws of Hawaii 1935, as [4] amended from time to time (hereinafter referred to as the General Excise Tax Law); and with respect to any money representing a claim for the Territory for taxes pursuant to said General Excise Tax Law was a public accountant of the Territory of Hawaii within the meaning of Section 571 of the Revised Laws of Hawaii 1935.

III.

That plaintiff duly made monthly gross income tax returns for each of the months of October, 1942, to March, 1944, inclusive, and annual returns of gross income tax for each of the years 1942 and 1943, showing the matters and information required to be shown, and duly filed the same with the proper officers of the Territory of Hawaii in every respect in conformity with and in compliance with the laws of the Territory of Hawaii in that behalf made and provided, and duly paid the gross income tax on his gross income based on the amounts of gross income reported in said returns as and when the same were due and payable.

IV.

That on or about May 2, 1944, the proper officer of the Territory of Hawaii, upon whom rests the duty of assessing gross income tax, caused to be assessed an additional tax on gross income for the period beginning October 1, 1942, and ending December 31, 1942, in the amount of \$1,996.60, for the period beginning January 1, 1943, and ending December 31, 1943, in the amount of \$6,701.28, and for the period beginning January 1, 1944, and ending March 31, 1944, in the amount of \$1,728.07, a total of \$10,425.95; that the whole amount of such additional gross income tax so assessed was occasioned by increasing the gross income tax on account of retail sales and the gross income tax payable on account of such sales by the following amounts: [5]

	Gross Income	Tax
October 1 to December 31, 1942:		
Retail Sales to Post Exchanges.....	\$49,602.24	\$ 744.03
Retail Sales to Ship's Service Stores....	81,383.69	1,220.76
Other sales to the United States and/or its instrumentalities, departments, or agencies	2,120.40	31.81
January 1 to December 31, 1943:		
Retail Sales to Post Exchanges.....	\$155,266.67	\$2,329.00
Retail Sales to Ship's Service Stores....	291,044.42	4,365.67
Other Sales to the United States, etc.....	440.67	6.61
January 1, to March 31, 1944:		
Retail Sales to Post Exchanges.....	\$33,444.20	\$ 501.66
Retail Sales to Ship's Service Stores....	81,036.41	1,215.55
Other sales to the United States, etc.....	723.99	10.86

that the notices of proposed change in gross income

and/or consumption tax notifying plaintiff of the said additional assessment of said gross income tax for said periods were dated May 2, 1944, and were signed by W. Borthwick, Tax Commissioner, by T. Westly.

V.

That on May 2, 1944, or within a short period of time after said date, defendant demanded that plaintiff pay the said sum of \$10,425.95 as and for an additional assessment of gross income tax for the period October 1, 1942, to March 31, 1944.

VI.

That plaintiff, on May 14, 1944, pursuant to the aforesaid demand, involuntarily and under duress, and to avoid the heavy penalties for failure to pay the said tax within twenty-one (21) days from the date of the said notice of additional gross income and/or consumption tax assessment, paid the aforesaid sum of \$10,425.95 under protest, a copy of which protest is attached hereto, made a part hereof for every purpose, and is marked Exhibit "A." [6]

VII.

That the aforesaid sum of \$10,425.95 as additional assessment of gross income tax for the period October 1, 1942, to March 31, 1944, was wrongfully and illegally demanded and collected by defendant from plaintiff for the following reasons:

(1) That the amount of \$691,777.66 claimed by defendant as the additional amount taxable at the retail rate of $1\frac{1}{2}\%$ represents sales to United States Post Exchanges and Ship's Service Stores; and the amount of \$3,285.06 claimed by defendant as the additional amount taxable at the retail rate of $1\frac{1}{2}\%$ represents sales to the United States and/or other instrumentalities, departments or agencies;

(2) That said sales to the United States and/or its agencies or instrumentalities are exempt from gross income tax under the provisions of the General Business Excise Tax Law of the Territory of Hawaii under which the taxes in question are purported to be assessed;

(3) That the imposition of the gross income tax on such sales by defendant is in violation of Article I, Section 8, Clauses 12 and 13, of the Constitution of the United States in that said tax is a direct burden on the Federal Government in the exercise of its essential governmental power of raising and supporting armies and of providing and maintaining a Navy;

(4) That the imposition of said tax by the Territory of Hawaii retards, impedes and burdens the operation of constitutional laws duly enacted by Congress for the purpose of carrying into execution essential governmental powers vested in the Government of the United States, which is in direct violation of the provisions of said Article I, Section 8, Clauses 12 and 13, of the Constitution of the

United States, and Section 55 of the Hawaiian Organic Act; [7]

(5) That the imposition of said tax is in violation of the Fifth Amendment of the Constitution of the United States in that it deprives the taxpayer of property without due process of law;

(6) That said tax purports to be a tax on the privilege of engaging in the business of selling to the United States for essential governmental purposes, and as such it constitutes a tax on a privilege which the Territory of Hawaii does not confer, and thereby is in violation of the Fifth Amendment of the United States Constitution in that it deprives the taxpayer of property without due process;

(7) That the imposition of said tax violates Section 55 of the Hawaiian Organic Act in that it imposes a direct tax on the privilege of carrying on business with the United States, which is a subject beyond the legislative power of the Legislature of the Territory of Hawaii in that it is not a rightful subject of legislation and is inconsistent with the Constitution and laws of the United States;

(8) That in no event can the gross income from sales to the Ship's Service Stores or other agencies or instrumentalities of the United States be taxed at more than $\frac{1}{4}$ of 1% when such sales to said agencies or instrumentalities of the United States are for resale;

(9) That plaintiff is a person doing a legally

organized wholesale and jobbing business known to the trade as such and all of said sales were made to retail merchants or jobbers for purposes of resale;

(10) That the requirement that a retail merchant, to whom sales are made by a legally organized wholesale business, must be licensed in order that sales to such a person shall be taxable at the wholesale rate rather than at the retail rate [8] is an unreasonable and arbitrary classification contrary to the provisions of Article I, Section 8, Clauses 12 and 13, and of the Fifth Amendment of the Constitution of the United States in that it discriminates against sales to the United States and its agencies and instrumentalities and subjects to tax, at a higher rate, merchandise sold to federal agencies or instrumentalities for resale than similar goods sold to other persons, and in that it deprives taxpayer of property without due process.

VIII.

That no part of said \$10,425.95 has been repaid by defendant to plaintiff, and that the whole amount is now due, owing and unpaid; that this suit is brought pursuant to the provisions of Section 571, Revised Laws of Hawaii 1935, and every other provision of law thereto enabling.

IX.

That plaintiff is justly entitled to recover from defendant, after allowing all just claims and off-

sets, said sum of \$10,425.95, together with costs and interest on said sum as by law provided.

Wherefore Plaintiff Prays: That process issue out of this Honorable Court, citing defendant to appear and answer this Complaint, and that plaintiff have judgment against the defendant William Borthwick for the sum of Ten Thousand Four Hundred Twenty-five and 95/100ths Dollars (\$10,425.95), together with costs and interests upon said sum.

Dated at Honolulu, T. H., this 17th day of May, 1944.

THOMAS H. BRODHEAD,
d.b.a.

T. H. BRODHEAD CO.,
By SMITH, WILD, BEEBE &
CADES,

By /s/ MILTON CADES,
Attorneys for Plaintiff. [9]

Territory of Hawaii,
City and County of Honolulu—ss.

Milton Cades, being first duly sworn, on oath deposes and says: that he is a partner in the firm of Smith, Wild, Beebe & Cades, attorneys for the plaintiff named in the foregoing Complaint; that he has read the same, knows the contents thereof, and that the same is true to the best of his knowledge, information, and belief.

/s/ MILTON CADES.

Subscribed and sworn to before me this 17th day of May, 1944.

[Notarial Seal]

/s/ FRIEDA H. ROBERT,
Notary Public, First Judicial Circuit, Territory of Hawaii.

My commission expires June 30, 1945. [10]

EXHIBIT A

Smith, Wild, Beebe & Cades
Honolulu, T. H.

May 11, 1944

Mr. William Borthwick
Tax Commissioner and Tax Collector
Territorial Tax Building
Honolulu, T. H.

Dear Sir:

Thomas H. Brodhead, the general partner of T. H. Brodhead Co., a registered special partnership, hereinafter called the "taxpayer," hereby

acknowledges receipt of your notices dated May 2, 1944, entitled "First Notice of Proposed Change in Gross Income and/or Consumption Tax Assessment" for the following periods: October 1, 1942, to December 31, 1942; January 1, 1943, to December 31, 1943; and January 1, 1944, to March 31, 1944, in which the total additional gross income and/or consumption taxes to be assessed is \$10,425.95. In your notices you purport to increase the gross income taxable on account of retail sales, and the gross income tax payable on account of such sales, by the following amounts:

	Gross Income	Tax
October 1 to December 31, 1942:		
Retail Sales to Post Exchanges.....	\$49,602.24	\$ 744.03
Retail Sales to Ship's Service Stores....	81,383.69	1,220.76
Other sales to the United States and/or its instrumentalities, departments, or agencies	2,120.40	31.81
January 1 to December 31, 1943:		
Retail Sales to Post Exchanges.....	\$155,266.67	\$2,329.00
Retail Sales to Ship's Service Stores....	291,044.42	4,365.67
Other Sales to the United States, etc.....	440.67	6.61
January 1, to March 31, 1944:		
Retail Sales to Post Exchanges.....	\$33,444.20	\$ 501.66
Retail Sales to Ship's Service Stores....	81,036.44	1,215.55
Other sales to the United States, etc.....	723.99	10.86

You Are Hereby Notified that the taxpayer disputes and disagrees with said additional assessment and contends that his gross income subject to tax is not in excess of that returned by him. [11]

Taxpayer herewith remits to you the said sum of \$10,425.95 demanded by you, and hereby notifies you to hold and keep the said sum of \$10,425.95 in

accordance with law pending final determination of the right of the Territory to claim, receive and retain said sum or any portion thereof.

You Are Further Notified that the taxpayer is paying and does pay the said sum under protest on the following grounds:

I.

That the amount of \$695,062.72 which you claim as the additional amount taxable at the retail rate of 1½% represents sales to the United States and/or its instrumentalities, departments or agencies.

(a) Such sales are exempt from gross income tax under the provisions of the General Business Excise Tax Act under which the taxes in question are purported to be assessed. (Brodhead v. Borthwick, decided March 31, 1944 (Judge Matthewman, being Law No. 16956 in the Circuit Court of the First Judicial Circuit, Territory of Hawaii.)

(b) The imposition of a gross income tax on such sales by the Territory in any event is in violation of Article I, Section 8, Clauses 12 and 13 of the Constitution of the United States of America, in that said tax is a direct burden on the Federal Government in the exercise of its essential governmental power of raising and supporting armies and of providing and maintaining a Navy. The imposition of said tax by the Territory retards, impedes and burdens the operation of constitutional laws duly enacted by Congress for the purpose of carrying into execution essential governmental powers

vested in the Federal Government, which is in direct violation of the provisions of said Article I, Section 8, Clauses 12 and 13 of the Constitution of the United States of America.

(c) The imposition of said tax is in violation of the Fifth Amendment of the Constitution of the United States in that it deprives the taxpayer of property without due process of law. Said tax purports to be a tax on the privilege of engaging in the business of selling to the United States for essential governmental purposes. As such it constitutes a tax on a privilege which the Territory does not confer. The right of the United States to make purchases is derived from the Constitution and the right to make sales to the United States is not given by the Territory, nor is it dependent upon Territorial laws, but it results from the authority of the national government to choose its own means and sources of supply. For the Territory to lay a tax on transactions by which the United States secures the things which it desires and needs for governmental purposes is a violation of the Fifth Amendment in that it deprives the taxpayer of property without due process. [12]

(4) The imposition of said tax violates Section 55 of the Hawaiian Organic Act of the Territory of Hawaii in that it imposes a direct tax on the privilege of carrying on business with the United States, which is a subject beyond the legislative power of the Legislature of the Territory of Hawaii in that it is not a rightful subject of legislation and

is inconsistent with the Constitution and laws of the United States.

II.

Such sales to Post Exchanges and Ship's Service Stores are made for the purpose of resale by such stores and cannot be taxed at more than $\frac{1}{4}$ of 1%.

(a) Taxpayer is a person doing a legally organized wholesale and jobbing business known to the trade as such, and all of said sales were made to retail merchants or jobbers for purposes of resale.

(b) The requirement that a retail merchant to whom sales are made by a legally organized wholesale business must be licensed in order that sales to such a person shall be taxable at the wholesale rate rather than at the retail rate is an unreasonable and arbitrary classification contrary to the provisions of Article I, Section 8, Clauses 12 and 13, and the provisions of the Fifth Amendment of the Constitution of the United States in that it discriminates against sales to the United States and its agencies and instrumentalities and subjects to tax, at a higher rate, merchandise sold to federal agencies or instrumentalities for resale than similar goods sold to other persons, and in that it deprives taxpayers of property without due process.

The specific grounds of protest hereinbefore set forth and the objections urged to the assessment of additional tax are made without prejudice to the right of the taxpayer to urge additional objections to said assessment and additional grounds of pro-

test, and the taxpayer reserves unto himself all other matters of objections and exception to any grounds of protest against said additional assessments which may hereafter be presented to any court of competent jurisdiction in any proceeding which may be commenced to recover the money paid under protest or proceedings to adjust the claims for taxes.

Very truly yours,

T. H. BRODHEAD CO.

By /s/ THOS. H. BRODHEAD,
General Partner.

Receipt of the sum of \$10,425.95 which is paid under protest, and receipt of the foregoing protest is hereby acknowledged this 15th day of May, 1944.

WILLIAM BORTHWICK,
Tax Commissioner and Tax
Collector.

By /s/ T. WESTLY. [13]

[Title of Circuit Court and Cause.]

TERM SUMMONS

The Territory of Hawaii: To the High Sheriff of the Territory of Hawaii, or His Deputy; the Sheriff of the City and County of Honolulu, or His Deputy, or Any Police Officer in the Territory of Hawaii Making Service Hereof:

You Are Commanded to summon the above named Defendant, in case shall file written answer Within Twenty Days After Service Hereof, to be and appear before the First Circuit Court at the Judiciary Building in Honolulu, at the term thereof pending immediately after the expiration of twenty days after service hereof; To Show Cause why the claim of the above named Plaintiff should not be avoided pursuant to the tenor of the annexed complaint.

And have you then there this Writ with full return of your proceedings thereon.

Witness the Honorable Presiding Judge of the Circuit Court of the First Judicial Circuit at Honolulu aforesaid, this 18th day of May, 1944.

[Seal] /s/ F. A. HONG,
Clerk.

SHERIFF'S RETURN

Served the within Summons William Borthwick, Tax Commissioner and Tax Collector, at Honolulu this 18th day of May, 1944, by delivering to him a certified copy hereof and of the complaint hereto

annexed and at the same time showing him the original.

Dated May 18, 1944.

/s/ SAM K. PAULO, SR.,

Deputy Sheriff, City and

County of Honolulu. [14]

General Order No. 133, Section 2, Paragraph 4

4. (a) No judgment by default shall be entered against any person who is in the Army, Navy, Marine Corps, or Coast Guard of the United States. No judgment by default shall be entered against any person employed or engaged in any occupation, business, or activity under the supervision or direction of the Military Governor, or otherwise essential to the national defense, until seven (7) days shall have elapsed after the return day provided in the summons or by the statutes of the Territory of Hawaii. A default judgment hereafter entered shall be set aside upon the mere request of the defendant or his attorney, made either orally or in writing, to the court, or clerk thereof, in which the case was pending at the time of the entry of such judgment, if such request be so made within fifteen days after entry of such default judgment. Leave to appear or answer shall be allowed or extended for a like period of fifteen days after such default shall have been set aside. In the event the defendant, after having been allowed to so appear or answer as aforesaid, shall fail to so appear or answer as aforesaid within said period of fifteen days, the

court may again enter or cause to be entered the default of the defendant and enter or order entered judgment by default against such defendant. A defendant shall have no right upon his mere request to have a default judgment set aside a second time in the same case.

(b) The provisions contained in this paragraph shall apply to pending cases as well as to cases hereafter commenced or instituted.

(c) A verbatim copy of the contents of this paragraph shall be attached to the summons and served upon the defendant or defendants in cases hereinafter commenced or instituted.

[Amending General Order No. 29]

[Endorsed]: Filed May 18, 1944. [14a]

[Title of Circuit Court and Cause.]

ANSWER

Comes now William Borthwick, Tax Commissioner of the Territory of Hawaii, defendant above named, by Rhoda V. Lewis, Assistant Attorney General of the Territory of Hawaii, answering the plaintiff's complaint heretofore filed in the above cause says:

I.

That he admits the allegations contained in paragraph II of said complaint.

II.

That except for the allegations contained in paragraph II, defendant denies all of the material allegations contained in plaintiff's complaint. [16]

Wherefore, defendant prays that plaintiff take nothing by his action.

Dated at Honolulu, T. H., this 25th day of May, 1944.

WILLIAM BORTHWICK,
Tax Commissioner of the Territory of Hawaii,
Defendant.

By /s/ RHODA V. LEWIS,
Assistant Attorney General of the Territory of
Hawaii.

[Endorsed]: Filed May 25, 1944. [17]

[Title of Circuit Court and Cause.]

STIPULATION

It Is Hereby Stipulated by and between Thomas H. Brodhead, doing business as T. H. Brodhead Co., plaintiff above-named, and William Borthwick, Tax Commissioner of the Territory of Hawaii, defendant above-named, by their respective counsel that:

I.

Plaintiff is and at all times hereinafter mentioned was a resident of Honolulu, City and County

of Honolulu, Territory of Hawaii; plaintiff is the general partner of a registered special partnership doing business in Honolulu aforesaid under the firm name and style of T. H. Brodhead Co.

II.

Defendant is and was at all relevant times the duly appointed, qualified and acting Tax Commissioner of [19] the Territory of Hawaii, and as such is and was at all relevant times in charge of the administration and enforcement of Act 141 (Ser. A-44) of the Session Laws of Hawaii, 1935, as amended from time to time (hereafter referred to as the General Excise Tax Law), and with respect to any money representing a claim of the Territory for taxes pursuant to said General Excise Tax Law (hereafter referred to as gross income taxes) was a public accountant of the Territory within the meaning of Section 571 of the Revised Laws of Hawaii, 1935.

III.

Plaintiff made monthly gross income tax returns for each of the months of October, 1942, to March, 1944, inclusive, and annual returns of gross income tax for each of the years 1942 and 1943, at the times required by law; plaintiff duly paid the gross income tax on the amounts of gross income reported in said returns as taxable, as and when the same was due and payable.

On April 26, 1944, plaintiff, with the permission of the Tax Commissioner, filed amended returns covering the periods of October 1 to December 31,

1942, January 1 to December 31, 1943, and January, February and March, 1944.

On May 2, 1944, the Tax Commissioner issued first notices of proposed additional assessments of gross income taxes for the aforesaid periods, increasing the gross income taxable and the tax thereon, as follows: [20]

October 1 to December 31, 1942

Business Activity	Additional Amt. Taxable	Rate	Additional Tax	
Retail Sales				
Post Exchanges.....	\$ 49,602.24	1½%	\$ 744.03	
Retail Sales				
Ships' Service Stores..	81,383.69	1½%	1,220.76	
Retail Sales				
Other Federal Sales—	2,120.40	1½%	31.81	
			<hr/>	\$1,996.60

January 1 to December 31, 1943

Retail Sales				
Post Exchanges.....	\$155,266.67	1½%	\$2,329.00	
Retail Sales				
Ships' Service Stores..	291,044.42	1½%	4,365.67	
Retail Sales				
Other Federal Sales....	440.67	1½%	6.61	
			<hr/>	\$6,701.28

January 1 to March 31, 1944

Retail Sales				
Post Exchanges.....	\$ 33,444.20	1½%	\$ 501.66	
Retail Sales				
Ships' Service Stores..	81,036.44	1½%	1,215.55	
Retail Sales				
Other Federal Sales....	723.99	1½%	10.86	
			<hr/>	1,728.07

Total Tax\$10,425.95

The aforesaid sales were reported by plaintiff but the income therefrom was claimed to be exempt as derived from sales to the United States government and its post exchanges and ships' service stores; moreover, plaintiff classified the sales to the post exchanges and ships' service stores as "wholesaling." The Tax Commissioner disallowed the claimed exemption and disallowed the wholesale [21] classification of sales to post exchanges and ships' service stores, reclassifying the same as retail sales.

On May 15, 1944, the plaintiff waived the necessity of a thirty-day interval between the first and second notices of assessment, without prejudice to his claims, and the proposed additional assessments were made. On the same day, May 15, 1944, plaintiff paid under protest the sum of \$10,425.95 so assessed, a true copy of plaintiff's protest being annexed to the complaint as Exhibit "A," it being stipulated that the copy so annexed to the complaint shall have the same effect as if admitted in evidence.

IV.

Plaintiff made the sales to the United States government and its post exchanges and ships' service stores in the respective amounts and for the periods above set forth, and no gross income tax has been paid with respect thereto except the tax so paid under protest. The following is a summary of the figures set forth in paragraph III of this stipulation, the below summary further showing the 1943 sales divided between the period January 1 to April 30, 1943, and May 1 to December 31, 1943.

Item No.	Amount of Gross Income and Period	Source*	Rate of Tax Assessed, and Amount of Tax Paid Under Protest	How Returned by Plaintiff
1.	\$130,985.93 Oct.-Dec., '42	PX sales	1½% \$1,964.79	Wholesaling; exemption claimed.
2.	\$ 2,120.40 Oct.-Dec., '42	Sales to U.S.	1½% \$ 31.81	Retailing; exemption claimed.
3.	\$115,106.05 Jan.-April, '43	PX sales	1½% \$1,726.59	Wholesaling; exemption claimed.
4.	\$ 169.92 Jan.-April, '43	Sales to U.S.	1½% \$ 2.55	Retailing; exemption claimed.
5.	\$331,205.04 May-Dec., '43	PX sales	1½% \$4,968.08	Wholesaling; exemption claimed.
6.	\$ 270.75 May-Dec., '43	Sales to U.S.	1½% \$ 4.06	Retailing; exemption claimed.
7.	\$114,480.64 Jan.-Mar., '44	PX sales	1½% \$1,717.21	Wholesaling; exemption claimed.
8.	\$ 723.99 Jan.-Mar., '44	Sales to U.S.	1½% \$ 10.86	Retailing; exemption claimed.

*PX refers to sales to post exchanges and ships' service stores.

V.

Annexed hereto as Exhibits "B" and "C," with the same effect as if admitted in evidence, are copies of plaintiffs' amended returns for October 1 to December 31, 1942, January 1 to December 31, 1943, and January, February and March, 1944 (Exhibit "B"); and copies of the additional assessments made by the Tax Commissioner covering the afore-said periods (Exhibit "C").

VI.

The post exchanges to which reference is made in this stipulation are operated under army regulations, a copy of such regulations as revised March 19, 1943, being hereto annexed as Exhibit "D" with the same effect as if admitted in evidence; it is hereby stipulated that the Army regulations in effect during the period involved in this case were the same in all material respects as said Exhibit "D."

Such post exchanges do not differ materially from the post exchanges involved in *Standard Oil Co. v. [23] Johnson*, 316 U. S. 481, 86 L. Ed. 1611, June 1, 1942. At no time did any of said post exchanges have a license under the General Excise Tax Law of the Territory, Act 141 (Ser. A-44) of the Session Laws of Hawaii, 1935, as amended, and at no time did any of said post exchanges pay any tax under said law.

Purchases are made by post exchanges both on the mainland and locally, according to the best judgment of the exchange officer, the delivered cost to the exchange being one of the most important factors considered.

Goods purchased from the plaintiff were purchased for sale by the exchange to authorized persons and organizations in accordance with paragraph 13 of the Regulations, which are Exhibit "D," and such authorized persons and organizations bought such goods from the exchange for their own use or consumption and not for further sale.

The post exchanges operate stores, as authorized

by paragraph 10 of the Regulations, Exhibit "D," and with the exception of goods sold to authorized organizations the goods bought from the plaintiff were sold in such stores in small quantities to each purchaser.

VII.

The ships' service stores, to which reference is made in this stipulation, have the same relation to the United States Navy as the post exchanges have to the United States Army and there is no material difference in the facts with respect to such ships' service stores.

VIII.

All of the evidence received upon the trial of L. No. 16956 on June 16, 1943, is hereby stipulated to be [24] equally applicable to this case, and the same shall be considered with the same effect as if received in this case.

IX.

This stipulation is not intended to be and is not a complete stipulation of facts, and each party reserves the right to produce evidence upon the trial of this cause; neither party by joining in this stipulation admits the materiality of the facts set forth herein, each reserving the right to argue that certain of such facts are immaterial to the disposition of this cause.

Dated at Honolulu, T. H., this 24th day of June,
1944.

THOMAS H. BRODHEAD, d.b.a
T. H. BRODHEAD CO.,
Plaintiff.

By SMITH, WILD, BEEBE &
CADES.

By /s/ MILTON CADES,
His Attorneys.

WILLIAM BORTHWICK,
Tax Commissioner,
Defendant.

By /s/ RHODA V. LEWIS,
Assistant Attorney General,
His Attorney.

Approved July 6, 1944.

/s/ JOHN ALBERT
MATTHEWMAN,
Judge. [25]

EXHIBIT "B"

TERRITORY OF HAWAII

FIRST TAXATION DIVISION

Combined Gross Income and
Consumption Tax Return

AMENDED

AMENDED

Thos. H. Brodhead-General Partner &
Bishop Trust Co., Trustee, Special
Partner d.b.a. T. H. Brodhead Co.
P. O. Box 675, and/or 843 Kaahumanu St.

No. 1- 591

1942

December

(FORM H-2-21) GROSS INCOME TAX - ACT 141 S. L. 1935. MONTH OF October to 1942

BUSINESS ACTIVITY	AMOUNT OF GROSS INCOME	EXEMPT INCOME	DEDUCTIONS	AMOUNT TAXABLE	RATE %	AMOUNT OF TAX
1. RETAILING	\$ 28,769.17	\$ 10.80 27,637.08	\$	\$ 1,121.29	1½	\$ 16.82
2. SUGAR PROCESSING AND CANNING					1½	
3. PRODUCING					¼	
4. WHOLESALE	239,567.53	218,497.57		21,069.96	¼	52.67
5. CERTAIN MANUFACTURING					¼	
6. PRINTING AND PUBLISHING ONLY					1½	
7. SERVICES OTHER THAN STRICTLY PROFESSIONAL					1½	
8. PROFESSIONAL SERVICES					1½	
9. CONTRACTING					1½	
10. THEATRES, AMUSE- MENTS AND RADIO BROADCASTING					1½	
11. INTEREST AND DISCOUNTS					1½	
12. COMMISSIONS	10,055.81			10,055.81	1½	150.84
13. RENTALS					1½	
14. ALL OTHER INCOME					1½	

14A. TOTAL GROSS INCOME TAXES \$ 220.33

CONSUMPTION TAX - ACT 160. S. L. 1935.

PROPERTY PURCHASED FOR USE OR CONSUMPTION	EXEMPTIONS	MONTHLY DEDUCTION	AMOUNT TAXABLE	
15. VALUE \$	\$	\$ 100.00	\$	1½

IMPORTANT: To be allowable, "Exempt Income" and "Deductions" claimed must be fully explained on the reverse side of this return.

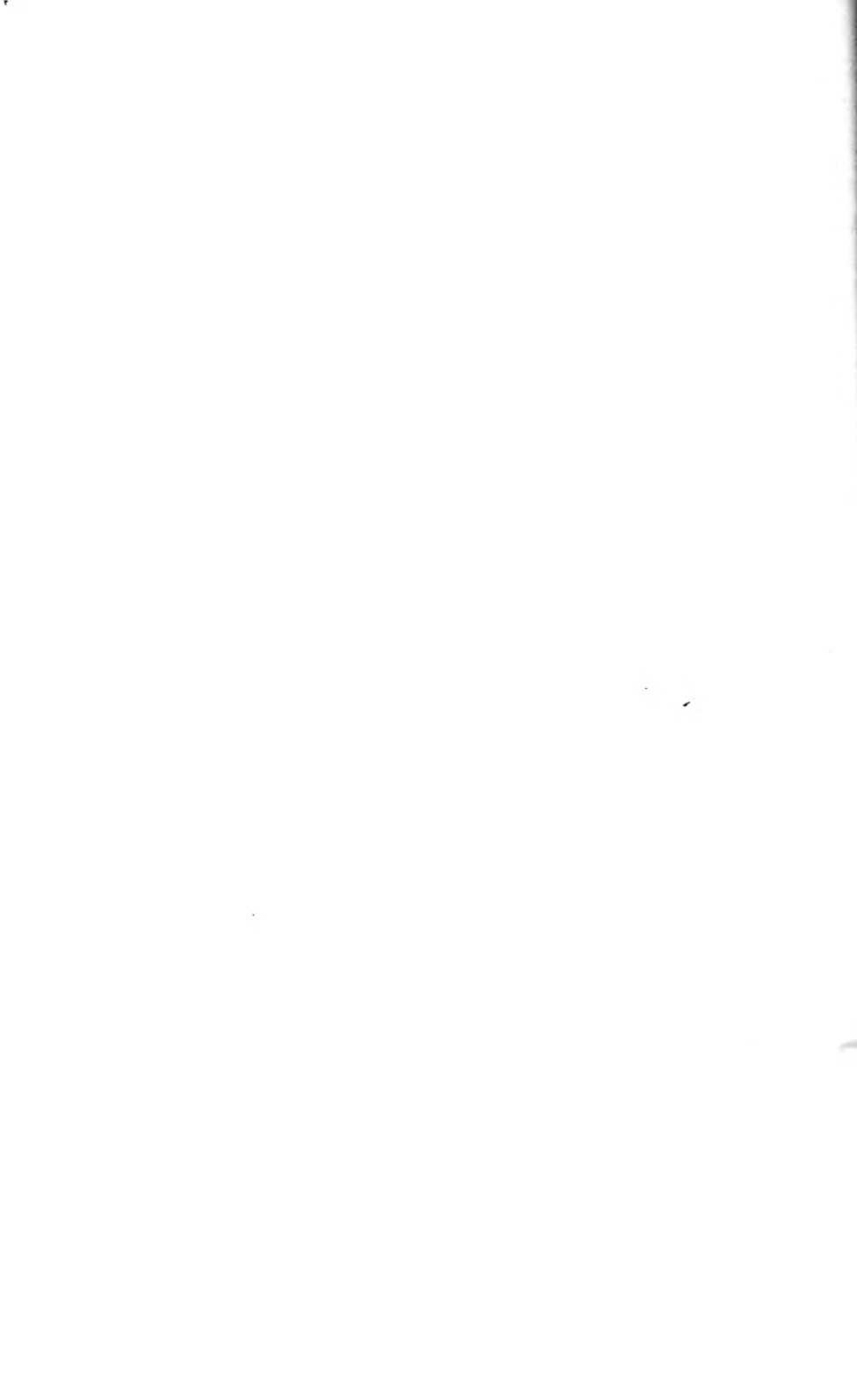
15A. TOTAL GROSS INCOME AND CONSUMPTION TAXES \$

16. DEDUCT "OVERPAYMENT"—If you have overpaid taxes and have received an OVERPAYMENT NOTICE accordingly, please deduct here and attach said notice to this return.	\$
--	----

DATE April 26th, 1944

16A. TOTAL AMOUNT DUE AND PAYABLE \$ 220.33

SIGNED T. H. Brodhead



EXEMPT INCOME

Sales to United States Government:

Mainland Delivery

\$ 25,516.68

Local Delivery

2,120.40

\$ 27,637.08

Sales to Post Exchanges:

Mainland Delivery

\$ 15,177.20

Local Delivery

49,602.24

Sales to Ship Service Stores:

Mainland Delivery

\$ 72,334.44

Local Delivery

81,383.69

\$218,497.57

Sales in Interstate Commerce

\$ 10.80



GROSS INCOME TAX AMENDEDANNUAL AMENDED

FIRST TAXATION DIVISION

DIVISION

Combined Gross Income and Consumption Tax Return
FOR PERIOD ENDING DECEMBER 31, 1943

LICENSE

NUMBER 00591

TERRITORY OF HAWAII

T. H. BRODHEAD, BISHOP TRUST CO., LTD., TR.

T. H. Brodhead Company

Name or Names of Owners Here

Firm Name Here

845 Kaahumanu St., Honolulu -16-Box 675, Honolulu -9

Street Address

Post Office

Kind of Business

Wholesale - Commission Merchant

Trade or Occupation

Check whether your books are kept on the CASH () or ACCRUAL () basis.

Individual ☐
Partnership ☒
Corporation ☐
Others ☐

GROSS INCOME TAX-ACT 141 S. L. 1935

→ (TAX OFFICE COPY)

BUSINESS ACTIVITY	(A) AMOUNT OF GROSS INCOME	(B) EXEMPT INCOME	(C) DEDUCTIONS	(D) AMOUNT TAXABLE	RATE %	(E) AMOUNT OF TAX
1. RETAILING	\$ 3,340.18	\$ 18.00 691.23	\$	\$ 2,630.95	1½	\$ 39.46
2. SUGAR PROCESSING AND CANNING					1½	
3. PRODUCING					¼	
4. WHOLESALE	695,957.71	613,462.21	755.83	81,739.67	¼	204.35
5. CERTAIN MANUFACTURING					¼	
6. PRINTING AND PUBLISHING ONLY					1½	
7. SERVICES OTHER THAN STRICTLY PROFESSIONAL		COPY			1½	
8. PROFESSIONAL SERVICES					1½	
9. CONTRACTING					1½	
10. THEATRES, AMUSEMENTS AND RADIO BROADCASTING					1½	
11. INTEREST AND DISCOUNTS					1½	
12. COMMISSIONS	32,124.44			32,124.44	1½	481.87
13. RENTALS					1½	
14. ALL OTHER INCOME					1½	
TOTALS						\$ 725.68

CONSUMPTION TAX-ACT 160. S. L. 1935.

PROPERTY PURCHASED FOR USE OR CONSUMPTION	EXEMPTIONS	MONTHLY DEDUCTION	AMOUNT TAXABLE	RATE
15. VALUE \$	\$	\$	\$	1½

RECONCILIATION

15A. TOTAL GROSS INCOME AND CONSUMPTION TAXES \$ 725.68

16. TOTAL GROSS INCOME TAXES PAID FOR THE PERIOD	\$ 725.68
17. TOTAL CONSUMPTION TAXES PAID FOR THE PERIOD	\$
18. ADDITIONAL ASSESSMENTS PAID FOR THE PERIOD	\$
19. AMOUNT OF TAXES AND ASSESSMENTS PAID FOR THE PERIOD	\$ 725.68

AFFIDAVIT

AMOUNT OF TAXES NOW DUE AND PAYABLE AND/OR OVERPAID \$

I (we) do swear or affirm to the best of my (our) knowledge and belief that this return and the schedules on the reverse side hereof and any supplemental schedules attached hereto constitute a true and complete return made in good faith for the period January 1, 1943 to December 31st, 1943 pursuant to the provisions of the General Excise Tax Law, Section 6, Act 141, Session Laws of Hawaii 1935.

Subscribed and sworn to before me this 26 day of April 1944.

/s/ Thomas H. Brodhead

Taxpayer's or Agent's signature

General Partner

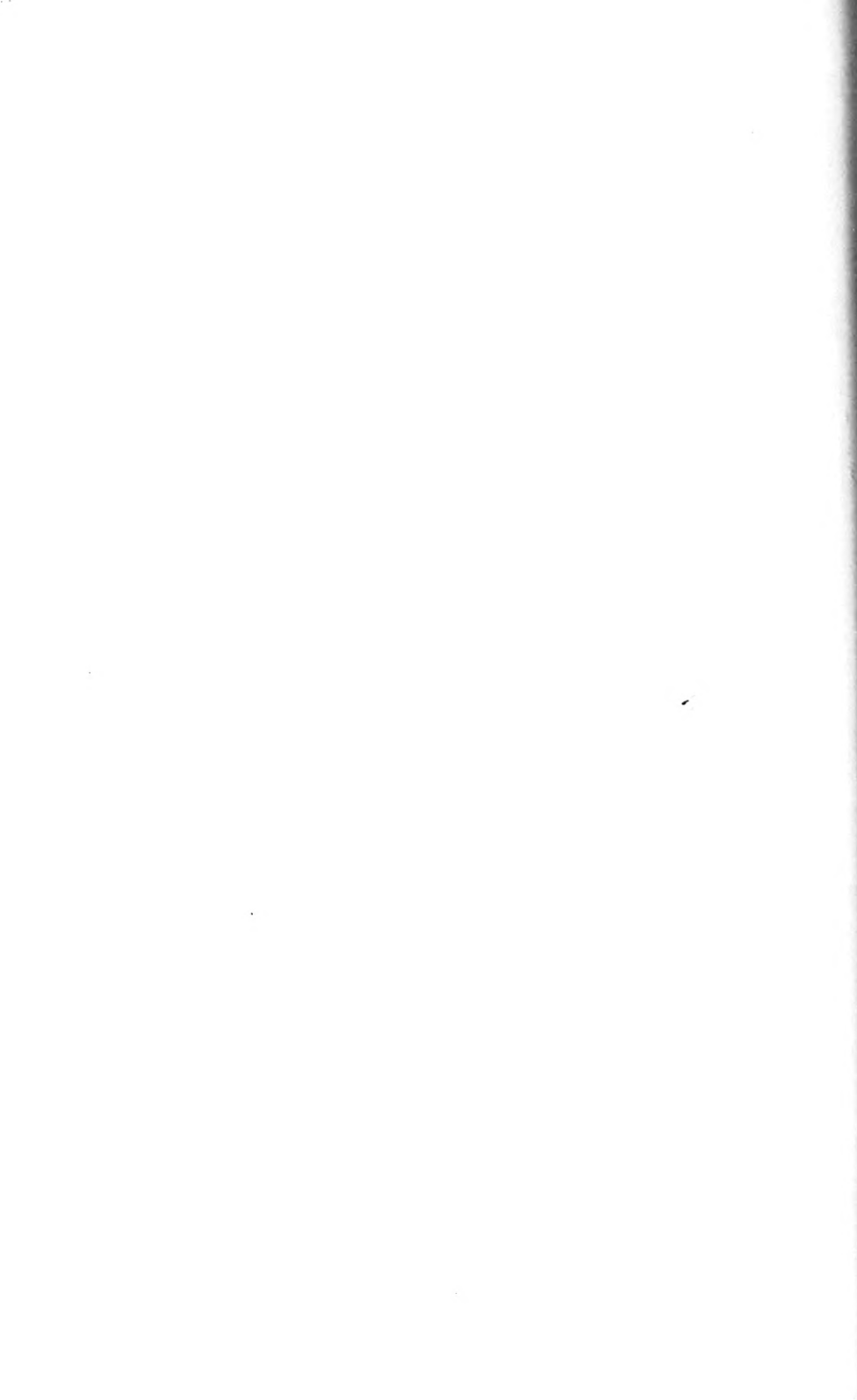
Signature of Officer Administering Oath

Title

Title

IN CASE OF A CORPORATION OR PARTNERSHIP, THIS RETURN MUST BE SIGNED BY AN OFFICIAL OR PARTNER.

(FORM H-600-61) 6



GROSS INCOME TAX: ACT 141 S. L. 1935

SCHEDULE "B"=EXEMPT INCOME:

DO NOT USE THIS SPACE		
	Date	Name
Ofc. Aud.		
Net Inc.		
Field Aud.		

Sales in Interstate and/or Foreign Commerce (Seattle, Wash.)			\$ 18.00
Interest received by Bldg. & Loan Associations from loans to its members			
	Mainland Delivery	Local Delivery	
SALES TO U. S. GOVERNMENT			
Sales to U. S. Government:	250.56	440.67	691.23
SALES TO POST EXCHANGES			
Sales to Post Exchanges:	12,193.69	155,266.67	167,460.36
SALES TO SHIP SERVICE STORES			
Sales to Ship Service Stores:	154,957.43	291,044.42	446,001.85
TOTAL EXEMPT INCOME			\$,614,171.44

SCHEDULE "C"=DEDUCTIONS:

Merchandise returned	\$	
Bad Debts charged off for Income Tax purposes if reporting on accrual basis - upon sales made on and after July 1, 1935 only (Attach schedule showing date incomes were reported on which taxes were paid)		755.83
Cash Discounts allowed and taken on sales		
Refunds to borrowers		
Territorial Gasoline Tax (at 5 1/4¢ per gallon on gasoline sold)		
Amounts paid to Sub-Contractors (Please attach list showing name, address, license number, type of work performed and amount paid to each sub-contractor)		
Discounts earned on Merchandise purchased, if your books show such as income		
Transportation Charges: (On Manufactured products shipped out of the Territory) (When shown as a separate item on the invoice and reimbursed by the purchaser of the merchandise)		
Inter-Departmental Transfers		
Trade-in Allowances		
All Other Deductions		
TOTAL DEDUCTIONS		\$ 755.83

CONSUMPTION TAX ACT 160 S. L. 1935

EXEMPTIONS: Purchases of Tangible Personal Property (not for use or consumption)	
DEDUCTIONS: Allowable deduction of \$100. for each month in which a Tax was paid.	

INSTRUCTIONS

THE BLUE COPY OF THIS RETURN SHALL BE TRANSMITTED TO THE TERRITORIAL TAX OFFICE. GROSS INCOME TAX DIVISION AND THE BUFF COPY SHALL BE RETAINED BY YOU.

EXEMPTIONS AND DEDUCTIONS

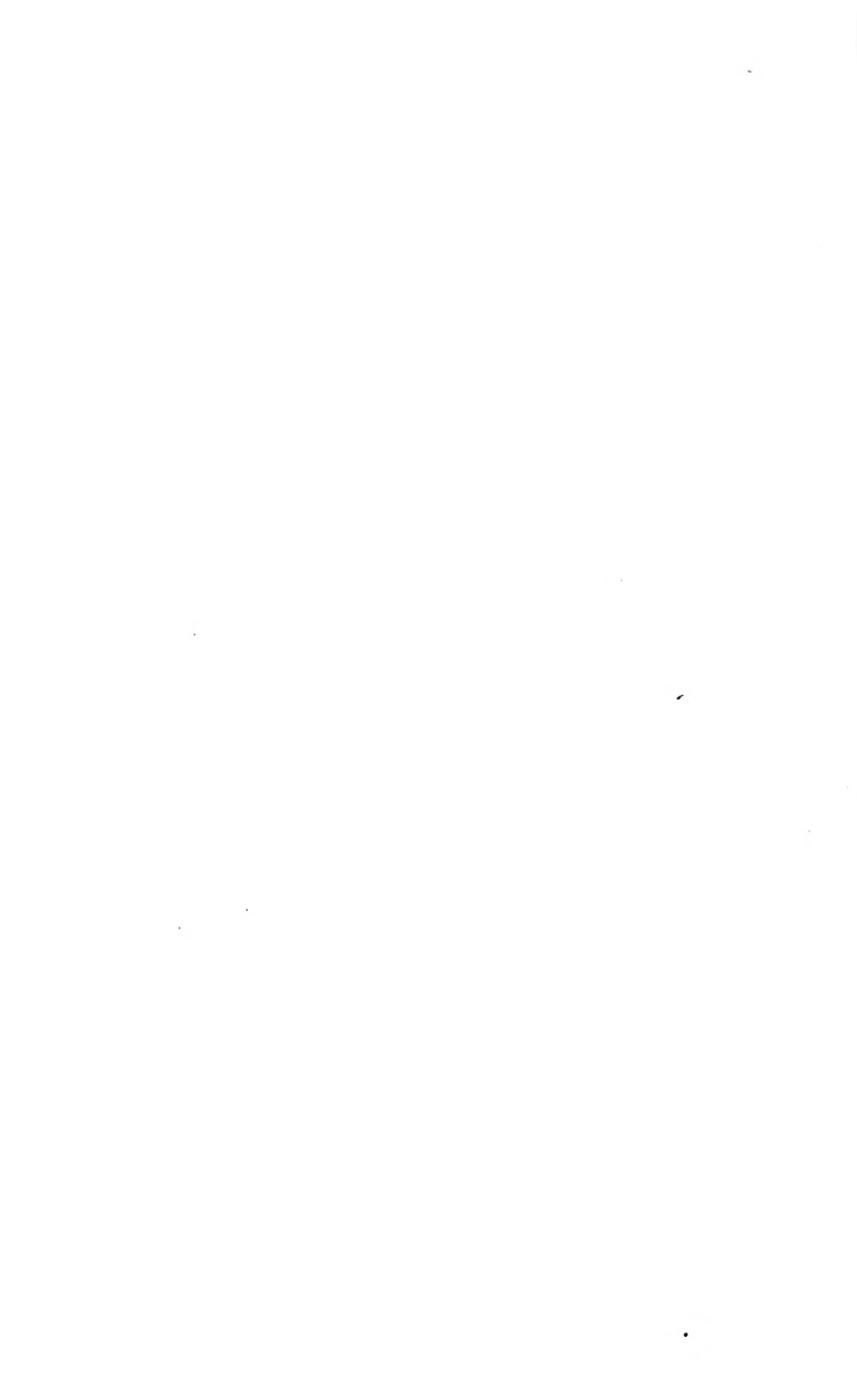
To be allowable, all Exemptions and Deductions must be fully explained. We therefore ask that you break down all the EXEMPT INCOME AND DEDUCTIONS which you claim in your return, and show in detail in the spaces provided above, why you are claiming such as EXEMPT INCOME or as DEDUCTIONS.

FILING OF RETURN

This report is for the period beginning January 1, 1943 to December 31, 1943, both inclusive, and shall be filed on or before March 20th 1944, if you report on a Calendar year basis. If you report on a FISCAL year basis then your ANNUAL RETURN shall be filed on or before sixty days after the time required for filing such return on a FISCAL basis.

CHANGE OF NAME OR ADDRESS

IF THE NAME OF YOUR BUSINESS HAS BEEN CHANGED DURING THE YEAR, OR YOU HAVE MOVED TO A NEW LOCATION, OR BOTH, PLEASE BE GOOD ENOUGH TO NOTIFY US SO THAT WE MAY CORRECT OUR RECORDS ACCORDINGLY.



FOR USE
DURING THE

TERRITORY OF HAWAII

FIRST TAXATION DIVISION

Combined Gross Income and Consumption Tax Return

YEAR Amended

T. H. Brodhead Co.

No.

1944

ONLY

843 Kaahumanu St.

Box 675

STREET ADDRESS

POST OFFICE

GROSS INCOME TAX—Act 141 S. L. 1935

MONTH OF

January

19

BUSINESS ACTIVITY	AMOUNT OF GROSS INCOME	EXEMPT INCOME	DEDUCTIONS	AMOUNT TAXABLE	RATE %	AMOUNT OF TAX
1. RETAILING	95.94			95.94	1½	1.44
2. SUGAR PROCESSING AND CANNING					1½	
3. PRODUCING					¼	
4. WHOLESALE	65,076.52	56,519.55		8,556.97	¼	21.39
5. CERTAIN MANUFACTURING					¼	
6. PRINTING AND PUBLISHING ONLY					1½	
7. SERVICES OTHER THAN STRICTLY PROFESSIONAL					1½	
8. PROFESSIONAL SERVICES					1½	
9. CONTRACTING					1½	
10. THEATRES, AMUSEMENTS AND RADIO BROADCASTING					1½	
11. INTEREST AND DISCOUNTS					1½	
12. COMMISSIONS	1,636.58			1,636.58	1½	24.55
13. RENTALS					1½	
14. ALL OTHER INCOME					1½	

14A. TOTAL GROSS INCOME TAXES

47.38

CONSUMPTION TAX—ACT 160. S. L. 1935.

PROPERTY PURCHASED FOR USE OR CONSUMPTION	EXEMPTIONS	MONTHLY DEDUCTION	AMOUNT TAXABLE	
15. VALUE \$	\$	\$ 100.00	\$	1½
<p>IMPORTANT: To be allowable, "Exempt income" and "Deductions" claimed must be fully explained on the reverse side of this return.</p>				
15A. TOTAL GROSS INCOME AND CONSUMPTION TAXES				\$
16. DEDUCT "OVERPAYMENT"—If you have overpaid taxes and have received an OVERPAYMENT NOTICE accordingly, please deduct here and attach said notice to this return.				\$

DATE April 26, 1944

16A. TOTAL AMOUNT DUE AND PAYABLE

SIGNED T. H. Brodhead



EXEMPT INCOME

Sales to Post Exchanges:

Mainland Delivery

.00

Local Delivery

\$16,113.66

Sales to Ship Service Stores:

Mainland Delivery

\$ 9,158.52

Local Delivery

31,247.37

\$56,519.55



FOR USE
DURING THE
YEAR **1944**
ONLY

TERRITORY OF HAWAII
Combined Gross Income and Consumption Tax Return

FIRST TAXATION DIVISION

T. H. Brodhead Co.
PRINT NAME AND ADDRESS EXACTLY AS SHOWN ON LICENSE
843 Kaahumanu St.

No.

Box 675

STREET ADDRESS

POST OFFICE

GROSS INCOME TAX—Act 141 S. L. 1935

MONTH OF **February**

1944

BUSINESS ACTIVITY	AMOUNT OF GROSS INCOME	EXEMPT INCOME	DEDUCTIONS	AMOUNT TAXABLE	RATE %	AMOUNT OF TAX
1. RETAILING	479.32			479.32	1½	7.19
2. SUGAR PROCESSING AND CANNING					1½	
3. PRODUCING					¼	
4. WHOLESALE	46,657.30	41,777.21		4,880.09	¼	12.20
5. CERTAIN MANUFACTURING					¼	
6. PRINTING AND PUBLISHING ONLY					1½	
7. SERVICES OTHER THAN STRICTLY PROFESSIONAL					1½	
8. PROFESSIONAL SERVICES					1½	
9. CONTRACTING					1½	
10. THEATRES, AMUSEMENTS AND RADIO BROADCASTING					1½	
11. INTEREST AND DISCOUNTS					1½	
12. COMMISSIONS	5,645.90			5,645.90	1½	84.69
13. RENTALS					1½	
14. ALL OTHER INCOME					1½	

*Supp. G. # 111-1608-20-1946
Date: 11-20-1946
Mark S. Simeone*

14A. TOTAL GROSS INCOME TAXES \$ 104.08

CONSUMPTION TAX—ACT 160. S. L. 1935.

PROPERTY PURCHASED FOR USE OR CONSUMPTION	EXEMPTIONS	MONTHLY DEDUCTION	AMOUNT TAXABLE	
15. VALUE \$	\$	\$ 100.00	\$	1½
IMPORTANT: To be allowable, "Exempt Income" and "Deductions" claimed must be fully explained on the reverse side of this return.				
15A. INCOME AND CONSUMPTION TAXES				\$
16. DEDUCT "OVERPAYMENT"—If you have overpaid taxes and have received an OVERPAYMENT NOTICE accordingly, please deduct here and attach said notice to this return				\$

DATE **April 26, 1944**

16A. TOTAL AMOUNT DUE AND PAYABLE \$

SIGNED **T. H. Brodhead**



EXEMPT INCOME

Sales to Post Exchanges:	
Mainland Delivery	.00
Local Delivery	\$13,215.60

Sales to Ship Service Stores:	
Mainland Delivery	5,113.67
Local Delivery	<u>23,447.94</u>

\$41,777.21



FOR USE
DURING THE
YEAR 1944
ONLY

TERRITORY OF HAWAII
Combined Gross Income and Consumption Tax Return

FIRST TAXATION DIVISION

AMENDED

T. H. Brodhead Co.

No.

PRINT NAME AND ADDRESS EXACTLY AS SHOWN ON LICENSE
843 Kaahumanu St., Box 675

STREET ADDRESS

POST OFFICE

GROSS INCOME TAX—Act 141 S. L. 1935

MONTH OF March

1944

BUSINESS ACTIVITY	AMOUNT OF GROSS INCOME	EXEMPT INCOME	DEDUCTIONS	AMOUNT TAXABLE	RATE %	AMOUNT OF TAX
1. RETAILING	968.91	867.99		100.92	1½	1.51
2. SUGAR PROCESSING AND CANNING					1½	
3. PRODUCING					¼	
4. WHOLESALE	51,562.07	48,456.10		3,105.97	¼	7.76
5. CERTAIN MANUFACTURING					¼	
6. PRINTING AND PUBLISHING ONLY					1½	
7. SERVICES OTHER THAN STRICTLY PROFESSIONAL					1½	
8. PROFESSIONAL SERVICES					1½	
9. CONTRACTING					1½	
10. THEATRES, AMUSEMENTS AND RADIO BROADCASTING					1½	
11. INTEREST AND DISCOUNTS					1½	
12. COMMISSIONS	6,637.00			6,637.00	1½	99.56
13. RENTALS					1½	
14. ALL OTHER INCOME					1½	

14A. TOTAL GROSS INCOME TAXES • 108.83

CONSUMPTION TAX—ACT 160. S. L. 1935.

PROPERTY PURCHASED FOR USE OR CONSUMPTION	EXEMPTIONS	MONTHLY DEDUCTION	AMOUNT TAXABLE	
15. VALUE \$	\$	\$ 100.00	\$	1½

IMPORTANT: To be allowable, "Exempt Income" and "Deductions" claimed must be fully explained on the reverse side of this return.

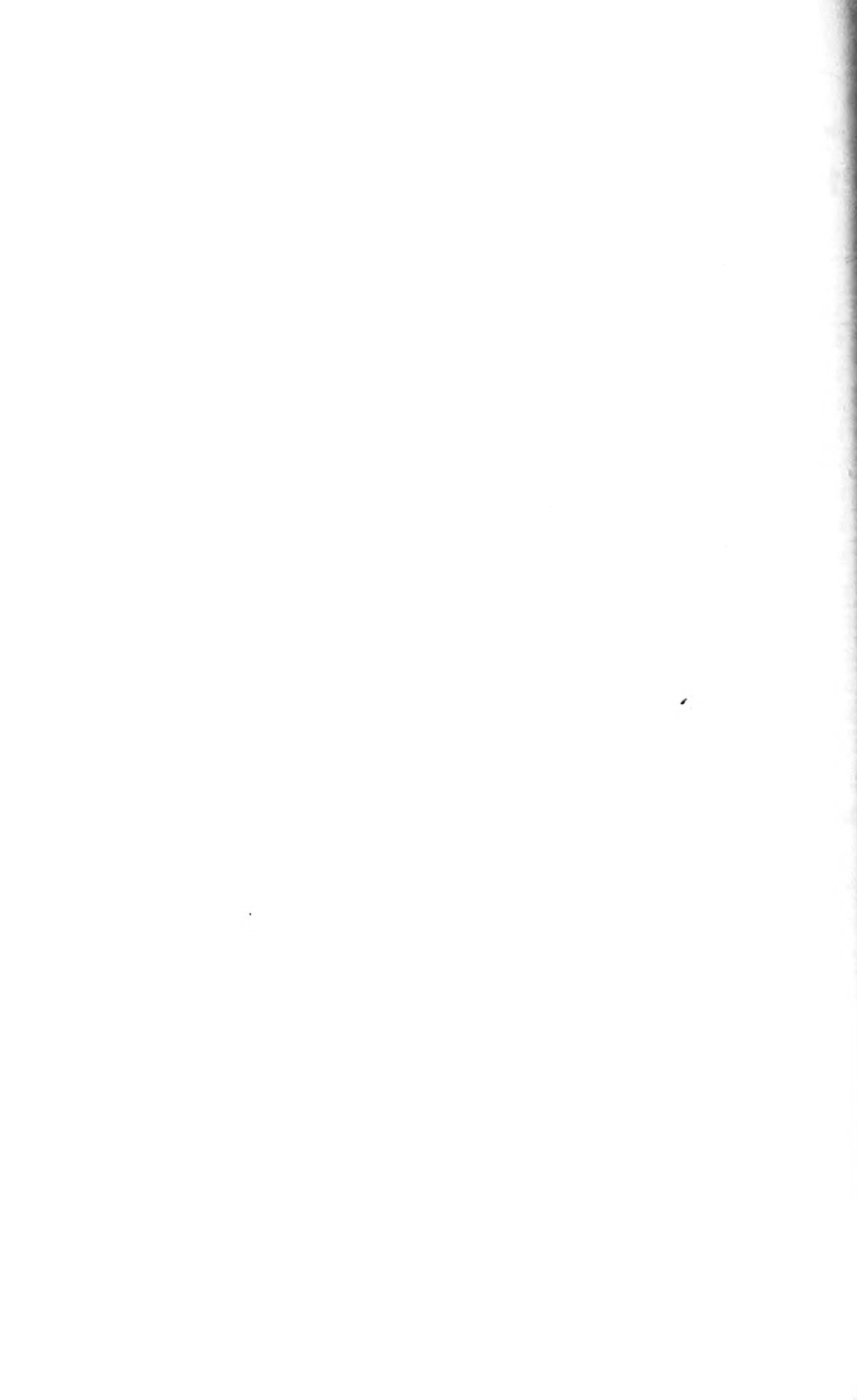
15A. TOTAL GROSS INCOME AND CONSUMPTION TAXES •

16. DEDUCT "OVERPAYMENT" — If you have overpaid taxes and have received an OVERPAYMENT NOTICE accordingly, please deduct here and attach said notice to this return. •

DATE April 26th, 1944

16A. TOTAL AMOUNT DUE AND PAYABLE •

SIGNED T. H. Brodhead



EXEMPT INCOME

Sales to U. S. Government:

Mainland Delivery	\$ 144.00
Local Delivery	723.99

Total	<u>\$ 867.99</u>
-------	------------------

Sales to Post Exchanges:

Mainland Delivery	% .00
Local Delivery	4,114.94

Sales to Ship Service Stores:

Mainland Delivery	18,000.03
Local Delivery	<u>26,341.13</u>

Total	<u>\$48,456.10</u>
-------	--------------------

(Endorsed): Filed Nov. 20, 1946.

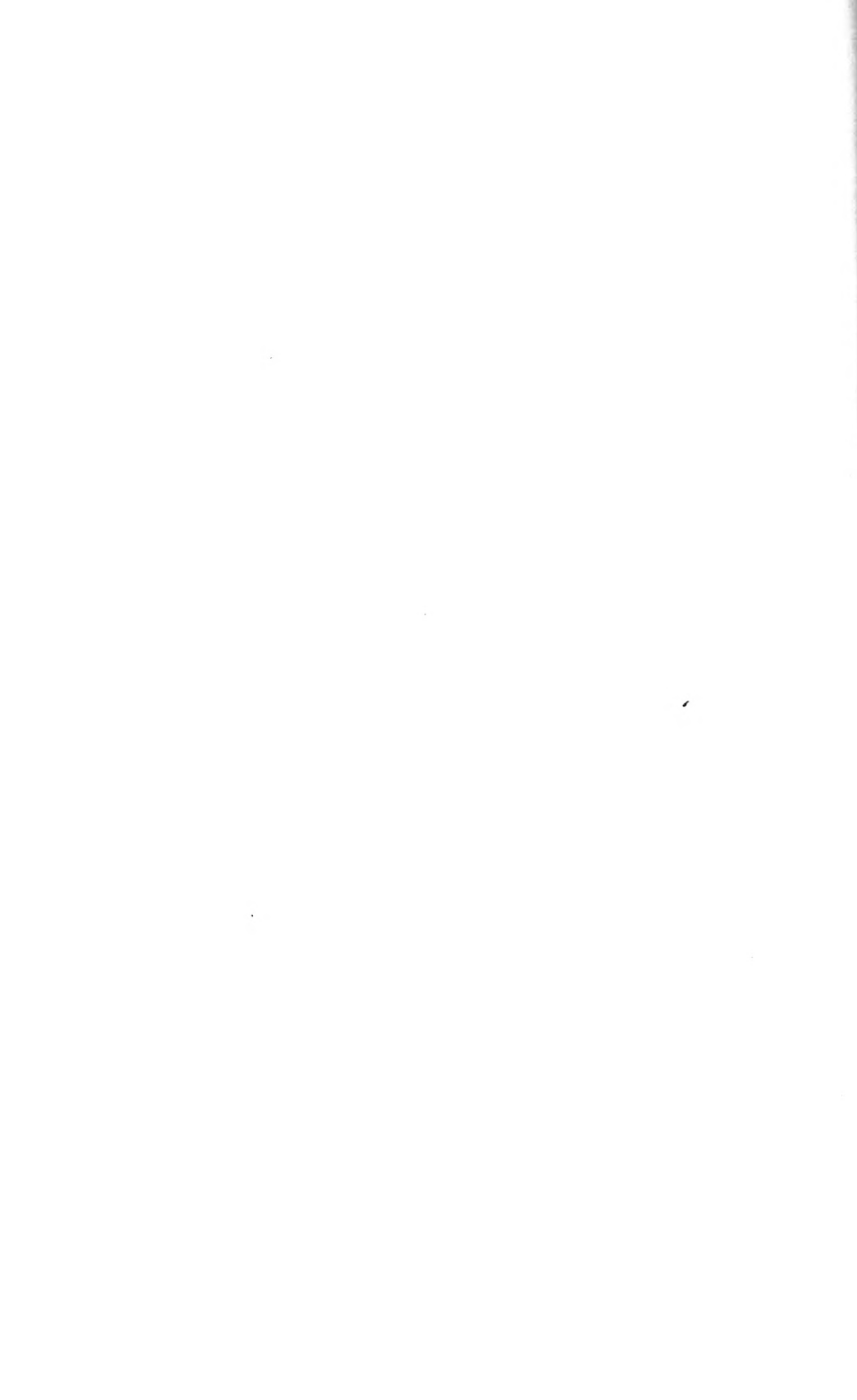


EXHIBIT "C"

Territory of Hawaii
TAX COMMISSIONER

Office of the Tax Assessor
1st Taxation Division

MAY 2 1944 194
Date of First Notice)

ASSESSORS' COPY OF NOTICE OF ADDITIONAL GROSS INCOME AND/OR CONSUMPTION TAX ASSESSMENT

For the period beginning October 1st 19 42

And ending December 31st 19 42

To: T. H. Brodhead Company

843 Kaahumanu Street

Honolulu -16- Hawaii

LICENSE
NUMBER: 591

ASSESSED: May 15, 1944

Business Activity	As Returned	As Changed	Additional Amount Taxable	Rate	Additional Tax
Retail Sales Post Exchanges			49,602 24	1-1/2	744 03
" " Ship's Service Stores			81,383 69	1-1/2	1,220 76
" " Other Federal Sales			2,120 40	1-1/2	31 81

TOTAL ADDITIONAL GROSS INCOME TAX TO BE ASSESSED \$ 1,996.60

CONSUMPTION TAX

Additional values of property bought for use or consumption	Exemptions	Monthly Deduction	Additional Amount Taxable	Rate	Additional Tax

TOTAL ADDITIONAL CONSUMPTION TAX TO BE ASSESSED

TOTAL ADDITIONAL GROSS INCOME AND/OR CONSUMPTION TAXES TO BE ASSESSED \$ 1,996.60

Explanation of proposed changes.

Disallowance of exemption claimed on sales to the Federal Government and its agencies exclusive of merchandise delivered and accepted on the Mainland.
Disallowed wholesale classification of sales to ship stores and Post Exchanges.

AUDITED BY:

J. I. Nishikawa

W. BORTHWICK Tax Commissioner

By: /s/ T. Westly

Handwritten notes:
Suff. # 2831
Oct 5-22-1944
A. M.
T. H. Brodhead
843 Kaahumanu Street
Honolulu, Hawaii



Territory of Hawaii

Office of the Tax Assessor

TAX COMMISSIONER

MAY 2 1944 194

First Taxation Division

Date of First Notice)

ASSESSORS' COPY OF NOTICE OF ADDITIONAL GROSS INCOME AND/OR CONSUMPTION TAX ASSESSMENT

For the period beginning January 1st 19 43And ending December 31st 19 43TO: T. H. Brodhead Company843 Kaahumanu Street

COPY

LICENSE
NUMBER: 591Honolulu -16- Hawaii

ASSESSED: May 15, 1944

Business Activity	As Returned	As Changed	Additional Amount Taxable	Rate	Additional Tax
Retail Sales Post Exchanges			155,266 67	1-1/2	2,329 00
" " Ship's Service Stores			291,044 42	1-1/2	4,365 67
" " Other Federal Sales			440 67	1-1/2	6 61

AL ADDITIONAL GROSS INCOME TAX TO BE ASSESSED \$ 6,701.28

CONSUMPTION TAX

Additional values of property bought for use or consumption	Exemptions	Monthly Deduction	Additional Amount Taxable	Rate	Additional Tax

AL ADDITIONAL CONSUMPTION TAX TO BE ASSESSED

ADDITIONAL GROSS INCOME AND/OR CONSUMPTION TAXES TO BE ASSESSED \$ 6,701.28

Explanation of proposed Changes:

Disallowance of exemption claimed on sales to the Federal Government and its agencies exclusive of merchandise delivered and accepted on the Mainland.

Disallowed wholesale classification of sales to ship's service stores and Post Exchanges.

ADDED BY:

J.I. Nishikawa

4 BORTHWICK, Tax Commissioner

By: /s/ T. Westly

Supp. G. #2631
4-11-44
A. M. B. B. B.
U.S. B. B. B.
Re. C. B. B. B.
S. M. B. B. B.

Territory of Hawaii

Office of the Tax Assessor

TAX COMMISSIONER

MAY 2, 1944 194

First Taxation Division

Date of First Notice)

ASSESSORS' COPY OF NOTICE OF ADDITIONAL GROSS INCOME AND/OR CONSUMPTION TAX ASSESSMENT

For the period beginning January 1st 19 44And ending March 31st 19 44TO: T. H. Brodhead Company843 Kaahumanu StreetHonolulu -16- Hawaii

LICENSE

NUMBER: 591

ASSESSED: May 15, 1944

No.	Business Activity	As Returned	As Changed	Additional Amount Taxable	Rate	Additional Tax
1	Retail Sales Post Exchanges			33,444	20 1-1/2	501 6
"	" Ship's Service Stores			81,036	44 1-1/2	1,215 8
"	" Other Federal Sales			723	99 1-1/2	10 8

TOTAL ADDITIONAL GROSS INCOME TAX TO BE ASSESSED \$ 1,728.0

CONSUMPTION TAX

Additional values of property bought for use or consumption	Exemptions	Monthly Deduction	Additional Amount Taxable	Rate	Additional Tax

TOTAL ADDITIONAL CONSUMPTION TAX TO BE ASSESSED \$

ADDITIONAL GROSS INCOME AND/OR CONSUMPTION TAXES TO BE ASSESSED \$ 1,728.0

Explanation of proposed Changes:

Disallowance of exemption claimed on sales to the Federal Government and its agencies exclusive of merchandise delivered and accepted on the Mainland.

Disallowed wholesale classification of sales to ship's service stores and Post Exchanges.

FILED Nov. 20, 1944
At 11:42 o'clock A. M.
Heath J. Krone
Clerk Supreme Court 2631

AUDITED BY:

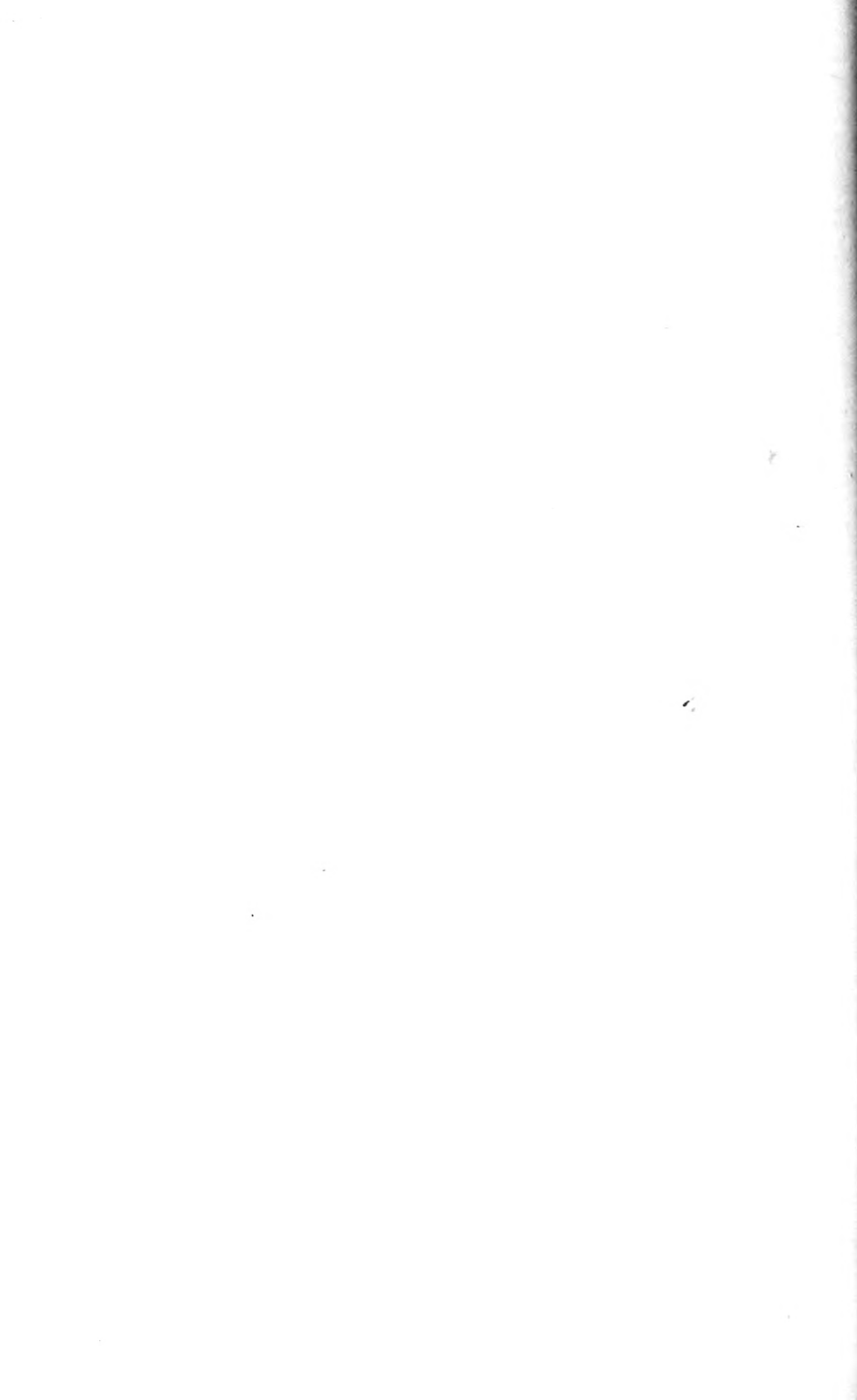
J. I. Nishikawa

W BORTHWICK, Tax Commissioner

By: /s/ T. Westly

S U M M A R Y

	<u>Post Exchanges</u>	<u>Ship's Service Stores</u>	<u>Other Federal Sales</u>
January	16,113.66	31,247.37	-----
February	13,215.60	23,447.94	-----
March	4,114.94	26,341.13	723.99
Total	<u>33,444.20</u>	<u>81,036.44</u>	<u>723.99</u>



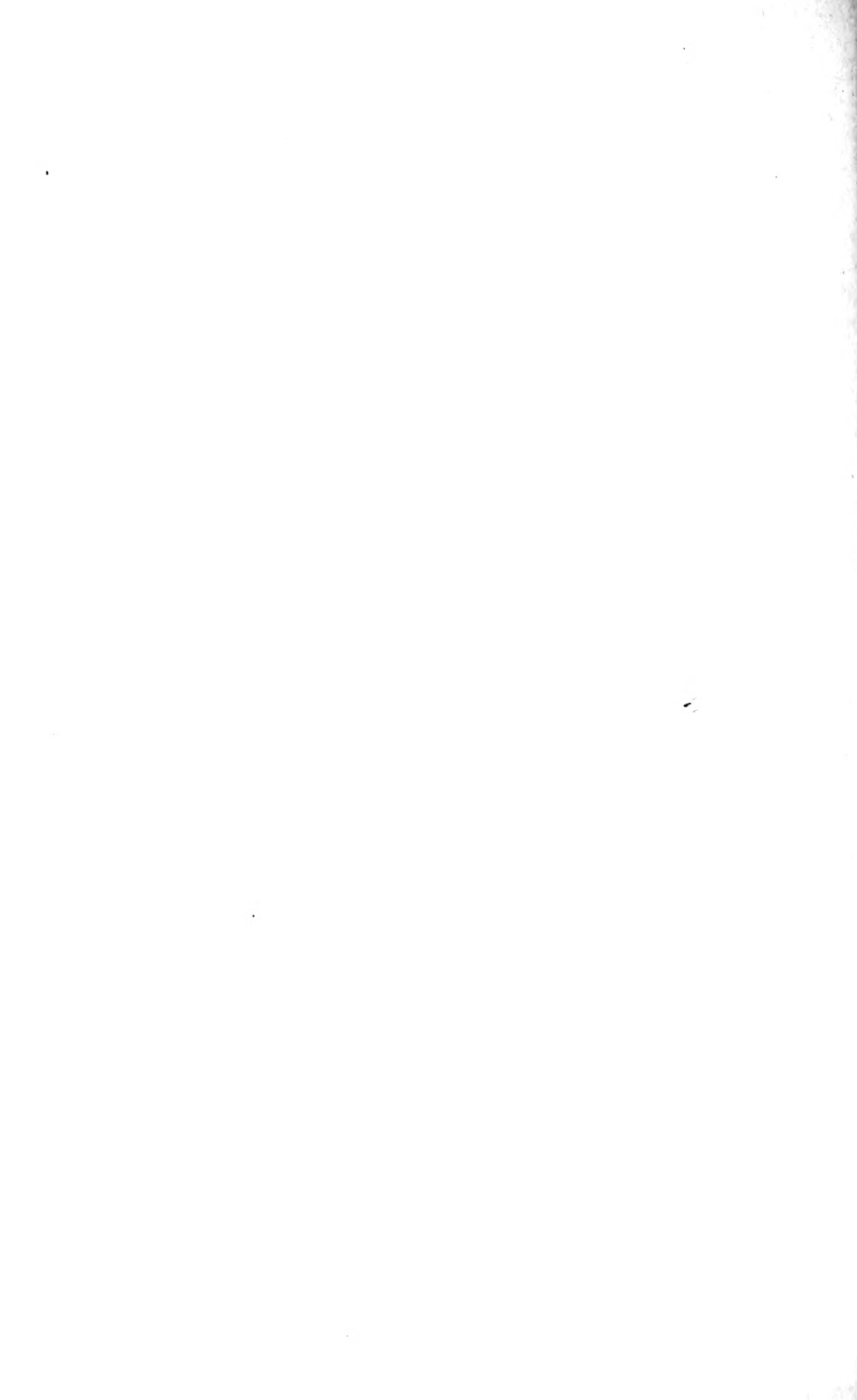


EXHIBIT D

Army Regulations

War Department

No. 210-65*

Washington, March 19, 1943

POSTS, CAMPS AND STATIONS

Army Exchanges

	Paragraphs
Section I. General	1-14
II. Personnel	15-21
III. Operations	22-35
IV. Miscellaneous	36-44

Section I

General

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*This pamphlet, together with Manual of Uniform System of Accounts, Forms and Accounting Procedure for Post, Camp, Station, and Field Exchange, supersedes AR 210-65 (Tentative), July 1, 1941, including C 1, August 22, 1942, C 2, October 12, 1942, C 3, December 30, 1942, and C 4, January 16, 1943; sections I, II, III and IV, Circular No. 124, War Department, 1941; section I, Circular No. 143, section IV, Circular No. 198, and paragraphs 1 to 3, inclusive, section VI, Circular No. 356, War Department, 1942.

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1. Applicability of regulations. These regulations will govern the operation of all exchanges established within the Army.

2. Definitions. a. An Army exchange is a military organization established as a part of the Army which supplies merchandise and services to specified persons and organizations.

b. An Army exchange is composed of such departments and maintains such activities and facilities as may be authorized.

c. As used in these regulations, the designation, commanding general of service command, will also include commanding generals of departments, theaters of operations, independent task forces, and any other commands the exchange service of which has been exempted by the War Department from the jurisdiction of the commanding general of the service command.

3. Purposes. Exchanges are established for the following purposes:

a. To supply the persons to whom sales are authorized (par. 13) at the lowest possible prices with articles of necessity and convenience not supplied by the Government except as provided in paragraph 10b(5).

b. To make available from profits funds which may be used to afford to military personnel additional facilities for comfort, recreation, and amusement, and to contribute to activities which will foster and increase the physical and spiritual welfare of military personnel.

4. Establishment. a. The commanding general of the service command will have general supervision over the establishment of exchanges. Army Exchange Service will be notified of the establishment of any exchange.

b. Whenever conditions make it desirable and practicable, the commanding officer of a post, camp, station, or installation will establish and maintain an exchange, to include such number of branches, departments, and subordinate activities thereof as may be necessary to serve the military personnel. The establishment of an exchange is authorized only at posts, camps, stations, or installations where enlisted personnel are on duty.

c. Except when the facilities of the home station exchange established under the provisions of b above are available, the commanding officer of troops in the field may authorize the establishment of exchanges when conditions make it desirable and practicable so to do. Where conditions render it necessary or desirable to establish an exchange at a location not included within any military reservation, the commanding officer of the organization desiring such an exchange will obtain prior approval of the commanding general of the service command.

d. A commanding general of a service command

may, where advisable and with consent of the Chief of Army Exchange Service, combine two or more independent exchanges serving separate posts, camps, stations, or installations and operate such combination as an exchange.

e. Except when governed by the provisions of b, c or d above and when no other exchange facilities are available, company or detachment exchanges may be established. In such cases they will conform as far as practicable, as determined by the commanding general of the service command, to these regulations.

f. The establishment of exchanges by or for troops traveling on water carriers is prohibited.

g. In any post, camp, station or installation but one exchange will be established. See paragraph 10.

h. Except for the operations of post restaurants as provided in AR 210-100, the establishment or operation as a civilian installation of any of the activities which an exchange is authorized to operate under the provisions of paragraph 10 is prohibited.

5. Designation. The designation of an exchange will identify it with the command it serves and all of its business will be transacted in the name of the exchange only. Examples:

Fort Snelling Exchange, or
17th AA Battery Exchange, or
501-1 Exchange.

By.....

Captain, AUS, Exchange Officer.

6. Capital for establishment. When the establishment of an exchange has been decided upon, the

commanding officer of the post, camp, station or installation will determine the amount of capital required. For loans see paragraph 35.

7. Liquidations. a. The commanding general of the service command will have general supervision over the liquidation of exchanges. Army Exchange Service will be notified of the liquidation of any exchange.

b. Complete liquidations.

(1) When a post, camp, station, or installation ceases to function as a Federal military activity all of the exchange assets will be liquidated and all of the ascertainable liabilities will be paid in full. Before the fixed assets are disposed of, the Army Exchange Service will be informed in detail of the amount and terms of the bids received for such assets and of the cost, length of service, and condition of each item. The Army Exchange Service, if it so desires, may become the preferred bidder for all or any part of the assets.

(2) The residue (proceeds after all liabilities are paid in full) will be remitted to the Army Exchange Service, to be disposed of as may hereafter be prescribed by the War Department upon recommendation of the Chief of Army Exchange Service.

(3) The records of a liquidated exchange will be deposited by the exchange officer with his immediate superior and will be disposed of by such officer as provided in paragraph 22g and h.

c. Partial liquidations. Whenever by reason of the decrease in personnel present at any post, camp, station, or installation, the amount of funds or

assets is greater than the amount required for current operation on a proportionately reduced basis, the commanding officer will report such facts to the commanding general of the service command who will direct the amount of such assets that will be retained by the exchange for its current operation. The commanding general of the service command will further direct that all assets over that amount be converted into cash and disposed of as provided in b (2) above.

d. Liquidation of exchanges outside of United States. Army Exchange Service will prescribe the procedure governing the liquidation of exchanges located outside the continental limits of the United States, provided that such procedure will be basically consistent with the provisions of b and c above.

8. Legal status. a. The legal status, rights, and liabilities of Army exchanges, exchange funds, property and personnel, commanding officers, exchange councils and exchange officers, and the rights as to litigation are determined by statute, the decisions of the Courts, the opinions of the Attorney General, and the Judge Advocate General of the Army. Subject to the foregoing and to these regulations, the Chief of Army Exchange Service is authorized to establish by interpretation the policy of the War Department upon the subjects noted. The Chief of the Army Exchange Service will distribute to exchange and other interested officers, in an appropriate manner, the necessary information

and procedures to insure understanding of such status, rights and liabilities.

b. Exchange operations will be governed by the policy interpretations based upon such decisions and opinions.

9. Exchange buildings and utilities. a. On military reservation.

(1) At posts, camps, stations, or installations where exchange buildings have not been provided from funds made available by the War Department, facilities may be secured by one of the following methods:

(a) The commanding officer will set apart for the use of the exchange any suitable public building or rooms available, or

(b) With the approval of the commanding general of the services command he may authorize the rental of any private building or part thereof on the reservation, the rental to be paid from exchange funds.

(2) Public or temporary buildings occupied by exchanges will be maintained by the post engineer out of funds applicable to the maintenance and operation of buildings, structures, and utilities on the particular post, camp, station, or installation.

(3) Fuel, water and electric services in sufficient quantities to satisfy normal needs for lighting, space heating, drinking, and sanitation, including suitable apparatus therefor, will be supplied at Government expense to exchanges and exchange enterprises, but fuel, water, or electric services will not be supplied

at Government expense for the operation of cooking devices, mechanical equipment, refrigeration electrical appliances, washing, cleaning, or power machinery for such enterprises as restaurants, tailor shops, barber shops, shoe repair shops, or any other activities operated by the exchange or concessionaires.

b. Not on military reservation. When deemed necessary or desirable to establish an exchange as provided in paragraph 4c, the commanding officer of the organization or activity will obtain the approval of the commanding general of the service command for the location of such exchange and the leasing of necessary facilities. When funds are not available from other sources, rental may be paid for appropriate space as provided in a (1) (b) above.

c. New construction.

(1) When facilities cannot be secured as provided in a(1) above, or when conditions make additional facilities necessary which cannot be secured as provided in a(1) above, a temporary building of a type, plan and construction approved by the Chief of Engineers may be erected, using wholly or in part the labor of troops and Government materials, tools and facilities as may be necessary and available.

(2) The exchange council, with the approval of the commanding officer, may recommend use of exchange funds for the erection of such temporary building when other assistance is not rendered. Any appropriation for such purpose must be approved

by the commanding general of the service command prior to obligation.

(3) The commanding general of the service command is authorized to approve the location of a building to be constructed under the provisions of (1) above.

(4) Buildings erected by exchanges on military reservations with proper authority and solely at their expense remain their property and may be sold by the exchange when no longer needed, upon written authorization of the commanding officer.

(5) Authority of the Secretary of War is required to permit the erection of temporary buildings on military reservations by private individuals or commercial concerns. This authority is not required for construction by exchanges, or when construction contracts between private individuals or commercial concerns and the exchange specify that immediately upon completion of the buildings, title thereto passes to the exchange.

(6) The exchange council, with the approval of the commanding officer, may, when necessary, recommend use of exchange funds to make alterations or additions to a building, provided no appropriations will be made when the cumulative total for alterations or additions to such building exceeds \$1,000. Appropriation of amounts to be spent which exceed the \$1,000 total, as provided above, must have, prior to obligation, the approval of the commanding general of the service command who will be governed by applicable Government limitations or regulations.

10. Activities. a. Authorized activities. An ex-

change may include, when approved by the commanding officer, the following activities and facilities:

(1) Main store, including military clothing and equipment.

(2) Branches.

(3) Warehouses.

(4) Soda fountain.

(5) Beer bar.

(6) Meat market.

(7) Vegetable and grocery market.

(8) Gasoline filling station.

(9) Automobile garage and service station.

(10) Restaurant or cafeteria.

(11) Barber shop.

(12) Beauty parlor.

(13) Laundry.

(14) Watch repair shop.

(15) Radio repair shop.

(16) Tailor shop, including dry cleaning and pressing.

(17) Shoe repair shop.

(18) Photographic studio.

(19) Vending and amusement machines.

(20) Gymnasium, including equipment for outdoor athletics.

(21) Recreation rooms, including billiard and pool tables, bowling alleys, and equipment for other indoor games when not provided by other services.

(22) Library supplied with books and periodicals when not provided by other services.

(23) Theater in which motion pictures, ama-

teur dramatics, and other entertainment may be conducted, if not provided by other services.

(24) Publication of a periodical.

(25) Taxicab and bus operation, subject to the following limitations:

(a) Unless strictly confined to service personnel and civilian Government employees as passengers, an exchange is not authorized to operate a taxicab or bus transportation facility nor to compete in any manner with civilian enterprise in such activity.

(b) The exchange may enter into a separate contract with any taxicab or bus company operating on the post, camp, station, or installation under a revocable license from the post commander, under which contract the exchange agrees to act as agent for such company for the sale of tickets entitling the holder to transportation.

(c) Under the limitations of b(1) below, the contract under (b) above requires the permission of the commanding general of the service command.

(d) For its services as such ticket agent the exchange may receive a legal commission. This should not exceed 10 per cent of the sales price of such tickets, and no part of such commission may be rebated or allowed in any manner as a credit to the purchaser of such ticket.

(e) Under the limitations described in (a), (b), (c) and (d) above, exchange coupons of

equivalent money cost may be used by ticket purchaser either to obtain transportation tickets or to pay such transportation cost in any manner included within the terms of such contract.

b. Limitations on activities.

(1) Activities other than those enumerated in a above will not be added to the business of an exchange without obtaining approval, through the Chief of Army Exchange Service, of the War Department.

(2) Except at stations located outside the continental limits of the United States and subject to the provisions of paragraph 11c, articles for sale will be limited to those articles of necessity and convenience as the commanding officer of the post, camp, station, or installation or the commanding general of the service command may determine desirable in view of local conditions. See also paragraph 12a(7).

(3) In all cases where the exchange acts as a collection agency for either a civilian activity or a concessionnaire, its liability will be limited to that of an agent and it will not be bound to perform any part of the customer's contract either by the payment of money or otherwise.

(4) Field exchanges may sell supplies obtained from quartermaster stores at cost price plus overhead cost fixed by the Secretary of War.

(5) The sale to enlisted men of regulation trousers, shirts, caps, belts, ties, socks, underwear, insignia, including cloth insignia such as chevrons,

shoulder sleeve and other patch type insignia, is authorized. The sale of articles of the uniform, except those specified above, similar to or as substitute for those issued by the supply service of the Army is forbidden.

(6) The operation of any gambling device, such as punch boards, slot machines, etc., by or in any exchange or exchange activity is prohibited.

(7) The sale of or dealing in beer, wine, or any other intoxicating liquors by any person in any exchange or upon any premises used for military purposes by the United States is prohibited. Beer with an alcoholic content of not more than 3.2 per cent by weight is considered nonintoxicating. See paragraph 33g.

(8) A periodical published by an exchange will not carry paid advertising.

(9) An exchange will not accept any gift or subsidy which might, directly or indirectly, be calculated to cause a preference in the purchase or sale of merchandise.

c. Concessions.

(1) So far as is practicable all of the authorized activities of the exchange will be conducted by the exchange.

(2) Subject to the provisions of (3) and (4) below, and when unusual conditions warrant, concessions may be granted by the exchange officer with the consent of the commanding officer, only for the conduct of activities indicated in a(6) to 18, inclusive, above.

(3) Concessions will not be granted private

individuals, firms, or corporations to operate any of the activities of the type listed in (2) above without the approval of the commanding general of the service command, and if the furniture, fixtures and equipment necessary to operate any such activity are owned by the exchange, in the absence of extenuating circumstances, such approval will not be given.

(4) A concession contract will be approved only when it embodies the express provision that the concessionaire assumes complete liability for all local taxes applicable to the property, income and transactions of the concessionaire.

(5) Contracts with concessionaires will neither state nor imply that any rental is to be charged the concessionaire for occupancy of space in buildings or for the use of utilities or facilities on the military reservation except as provided in paragraph 9a(3). The contract will contain provisions that the post authorities retain supervision of the activities and control of prices to be charged.

(6) When concessions occupy real estate not under control of the exchange, a license or lease is required (AR 100-60 and 100-62).

(7) A concessionaire is in no sense an agent of the exchange and will not be permitted to represent himself as such the public by the use of the words "— Exchange" on letter or bill heads, signs, or in any other manner.

(8) The limitations imposed upon sales by exchanges apply equality to exchange concessionaires.

d. Vending and amusement machines.

(1) Vending and amusement machines may be installed in posts, camps, stations and installations by—

(a) Outright purchase for cash, or installment contract.

(b) Rental purchase.

(c) Loan.

(d) Rental.

(2) The negotiating agency for procuring vending and amusement machines at posts, camps, stations or installations will normally be the exchange.

(3) All vending and amusement machines installed on the post will be under the control of the exchange. Exception is made for those installed in hospitals, service clubs, and messes operated under the provisions of AR 210-60, for the benefit of the fund concerned, at the discretion of the post, camp, station or installation commanding officer, and except where specific War Department authority has been granted under the provisions of paragraph 8a(1), AR 210-50.

11. Army Exchange Service. a. The Army Exchange Service is that part of the Army which has jurisdiction over and provides staff supervision of the operation of all Army exchanges, and consists of such officers, enlisted men, and civilian personnel necessary to perform the functions assigned to it.

b. This Service will have jurisdiction over, and will be extended to, all exchanges of the Army through appropriate personnel on the staffs of commanding generals of service commands and commanding officers of posts, camps, stations and in-

stallations, at whose directions exchanges have been established.

c. With reference to all Army exchanges, the Army Exchange Service is charged with—

(1) Developing policies, plans, and procedures for and supervising the installation and operation of—

(a) A uniform and coordinated system of operating procedures, pricing policies, and merchandising methods, including the safeguarding of exchange funds and property, and the determination of permitted types of merchandise to be sold by exchanges.

(b) Personnel policies and procedures, to include insurance plans, in-service training programs and training of exchange officers.

(c) Accounting and auditing methods and procedures.

(d) Minimum and maximum percentages of gross profits, operating expenses, and net profits.

(e) The regulation of dividends.

(f) Determination of type of equipment and fixtures to be used by exchanges.

(g) Establishment of fees to be paid by exchanges to the Army Exchange Service for services enumerated herein.

(2) Performing the following functions:

(a) Providing and prescribing the use of purchasing and fiscal services.

(b) Obtaining price agreements from manufacturers and distributors on items purchased

by exchanges, and prescribing the use of such price agreements.

(c) Administrating all funds accruing to the Army Exchange Service.

(d) Negotiating for and providing funds to be loaned to exchanges under such regulations as the Chief of Army Exchange Service may prescribe.

(3) Transmitting to exchange officers and personnel in an appropriate manner necessary information as to all activities within the scope of the foregoing duties and functions.

(4) Exercising an advisory and policy-making function for the War Department in all other matters within the scope of the foregoing duties and functions.

12. Purchases. a. For exchange.

(1) Except as authorized in (a) and (b) below and paragraph 18o, all purchases of merchandise or other property will be made by the exchange officer who will notify all vendors on the purchase order, or by other appropriate means, that the contract is made with the exchange and not with the United States Government.

(a) Exception to the above requirement is authorized when, by reason of absence on other duty, the exchange officer may not advantageously make such purchases. In these cases the exchange office manager may, when specifically authorized by the commanding officer, make routine purchases in limited quantity.

(b) In large exchanges maintaining a pur-

chasing department and stock control system, routine replacement of lines of merchandise handled in the exchange may be made by the head of the purchasing department from a list of dealers authorized by the exchange officer.

(2) The exchange officer will, in all cases, be responsible for the purchase made by any subordinate as authorized in (1) (a) and (b) above.

(3) Purchases made verbally by the exchange officer, or as provided in (1) (a) and (b) above, will be confirmed by written purchase order immediately thereafter.

(4) Inventories will be held to a reasonable minimum.

(5) Purchases at prices in excess of those published in Army Exchange Service price agreements (par. 11c) are not authorized except to supply immediate needs to exchanges operating in the field, or in emergencies due to lost or delayed shipments or other like circumstances, or when procurement, delivery, or price considerations render it to the interest of the exchange to purchase from local distributors.

(6) (a) All purchases within the continental limits of the United States by exchanges located outside the continental limits of the United States will be made through Army Exchange Service.

(b) Commercial and financial transactions of any type within the United States by exchanges located outside the continental limits of the United States will be conducted only through Army Ex-

change Service in accordance with provisions prescribed by the Chief of Army Exchange Service.

(7) The purchase or sale by Army exchanges of articles of military uniform and equipment not in conformity with the provisions of AR 600-35 is forbidden.

b. For concessionaires. The purchase by the exchange of material needed by concessionaires in the operation of their concessions is permitted only after all taxes involved, if any, have been advanced by the concessionaire and when such material is not to be resold.

c. All goods or property purchased by or for the account of an exchange will be accounted for on its books.

d. No merchandise will be held on consignment or to be paid for by exchanges when sold. The provisions of this subparagraph will not be construed as prohibiting the established business practice of making an agreement, at the time of purchase, for the return to the vendor for credit of unsold seasonal merchandise at a specific time.

e. Restrictions on purchases.

(1) Purchases by the exchange of merchandise and equipment will be so regulated that, except as provided in (2), (3) and (4) below, the cash on hand and accounts receivable at any time will be sufficient to pay all invoices within the discount period and to pay other current liabilities as they become due.

(2) Purchases made during the first 3 months following the initial establishment of an exchange

may, when recommended by the council and approved by the commanding officer, be paid for not later than the 15th of the second month following such purchases.

(3) Except for transactions provided for in a (6) above, exchanges outside the continental limits of the United States may, on recommendation of the exchange council and approval of the commanding officer, deviate from the provisions of (1) and (2) above where conditions make such deviation necessary.

(4) The commanding officer upon recommendation of the exchange council may authorize the payment, by not to exceed 12 monthly payments, for equipment and fixtures for exchange operations. See paragraph 17b(12) and 33c. -

(5) In the establishment of new exchanges, the stock of merchandise and investment in equipment and fixtures will be held to a minimum consistent with efficient operation.

13. Sales. a. To whom made. Exchanges are authorized to sell to the following-named persons and organizations only. Purchases by individuals will be limited as hereinafter set forth.

(1) Personnel and organizations now or hereafter authorized by law and regulation to purchase subsistence stores or other quartermaster supplies as defined in paragraphs 2 and 6, AR 30-2290, may purchase at exchanges. Dependent members of the families of persons so authorized may act as agents for such persons upon proper identification.

(2) Civilians other than those above defined and

who are regularly employed or serving at military posts, camps, stations or installations may purchase for their own consumption on the post, upon proper identification, items of food, drink and tobacco products and no other merchandise of any kind.

b. Sales to Government. Sales to the Government by exchanges are authorized only in cases where the same class of service cannot be conveniently or reasonably obtained elsewhere and where a direct advantage will accrue to the Government from the method resorted to. In no case will an exchange or concessionaire bidding as such be permitted to enter into public competition or to submit bids in response to advertisements calling for proposals for furnishing supplies or services. When accounts are submitted for sales of the kind described, the vouchers will contain a full statement of the grounds upon which the sale of supplies or services was based and will fully set forth all the circumstances of the transaction with a view to enabling the proper agencies of the United States Government to determine whether such purchase was in the public interest.

c. Coupon books.

(1) The sale of coupon books for cash is authorized. The exchanges will make available coupon books to all branches and activities approved by the commanding officer.

(2) Coupon books when sold will show the name and organization of the patron and will be authenticated by the exchange representative making the

sale. Coupons will be accepted by the exchange or concessionaire only when presented undetached from the book by the person whom issued, except that a chaplain or surgeon may make purchases with detached coupons for men sick in the hospital. Any person who discovers counterfeit coupons or the misuse of coupons will immediately notify the exchange officer who will take appropriate action.

(3) When organizations are to be transferred from a post, camp, station, or installation, the exchange officer will make arrangements with the commanders of such organizations to redeem for cash the unused coupons in the hands of members of such organizations. If the time element involved in the transfer of troops from the post, camp, station or installation is such as to make impossible the immediate cash redemption of exchange coupons, the organization commander will collect such unused portions of coupon books and forward them to the exchange officer for a consolidated settlement. The organization commander, upon receipt of the redemption value, will make distribution to the individual members concerned.

(4) Coupon books will not be sold at a discount.

d. Credit sales.

(1) Exchanges are prohibited from making credit sales to individuals either of merchandise or coupon books.

(2) Organizations which are authorized to buy at exchanges are entitled to buy on credit.

e. Special orders. Exchanges may purchase by special order only for officers and enlisted personnel,

items of personal military necessity not usually carried in stock.

14. Profits. a. General. The commanding general of the service command is responsible that exchange profits are within the limits prescribed under the authority of paragraph 11c.

b. Funds available for distribution. The amount of cash and other liquid assets, except inventories, in excess of current liabilities, including due portions of notes or installment contracts, as shown on exhibit E of the monthly financial statement, is the amount of funds available for distribution, except that any funds in excess of the total accrued net profit since the date of the last financial statement upon the basis of which a distribution was made will not be available for distribution. Any departures from this method of determining funds available for distribution will be upon the recommendation of the exchange council and the commanding officer, and approved by the commanding general of the service command.

c. Participation by organizations.

(1) Batteries, companies, squadrons, troops and any other units organized under Tables of Organization, detachments, allotments to service commands, or exempted activities, except as provided for in (2) below, will participate in the net profits of an exchange if served by the exchange for a period of more than 10 days, provided that no organization will participate in any distribution of net profits where the share thereof is less than \$10.

Enlisted men being processed through a reception center will not be included in the average strength report of the organization for the distribution of exchange funds unless present for more than 10 days. An organization will cease to participate in such net profits from the date of its departure from the post, camp, station or installation unless served by such exchange or a branch thereof during its absence therefrom.

(2) Organizations passing through staging areas or ports of embarkation will not participate in exchange profits. The sales price of articles sold by exchanges at staging areas or ports of embarkation will be maintained at a minimum in order that benefits that would ordinarily accrue will be passed on to such organizations direct by the exchanges.

d. Distribution of funds. The exchange council, when recommending the distribution of available funds for approval of the commanding officer, will assure itself that exhibit E of the monthly financial statement is complete and, subject to any limitation imposed under the provisions of paragraph 11c will, after obtaining such approval, make disposition of all available funds currently and as provided below.

(1) Special reserves. To set aside limited cash reserves for projects, only in specific amounts and for specific purposes, such as anticipated expansion of exchange activities and addition to recreational and welfare activities.

(2) Appropriations. Such sums as the council

recommends and the commanding officer approves will be appropriated as follows:

(a) To the post, camp, station or installation recreation fund and to the Chaplain's fund as provided in AR 210-50.

(b) To the post band or to bands of member organizations, and to headquarters funds, which do not otherwise participate in exchange distributions, in accordance with a schedule provided or approved by the commanding officer.

(c) For the benefit of the entire garrison, such as laying out, preparing and cultivating gardens and necessary seeds, roots and plants exclusive of any commercial activity; purchase and maintenance of books, newspapers, periodicals, stationery, etc., for the exchange or post library; purchase of gymnasium equipment or outdoor athletic equipment for free use of the command, and for prizes for athletic competitions for the garrison or such other military organizations as may be temporarily quartered on the reservation.

(d) To the recreation fund for the purchase of furniture and equipment for day rooms in barracks. The furniture and equipment so purchased will remain the property of the post, camp, station or installation and will be for the free use of any units quartered in the barracks for which such room is equipped.

(e) Appropriations for purpose other than those listed above require the approval of the commanding general of the service command.

(3) To organization funds. An amount of available funds will be disbursed to participating organizations and detachments, in accordance with limitations prescribed under the authority of paragraph 11c (1) (e) and subject to the limitations of c above, prorated upon the basis of each organization's average morning report of present enlisted strength during the period since the date of the financial statement upon which the last distribution was made. The distribution herein contemplated will include proportionate distribution and payment to organizations that have departed the station during the accounting period except as provided in c above.

(4) Contingency reserve. Any amount remaining after distribution as provided in (1) to (3), inclusive, above, will be placed in a contingency reserve and should be invested in obligations of the United States Government.

(5) Payment to departed organizations. Payment to organization funds of the amount determined under (3) above or the payment of any other indebtedness due to organizations that have left the continental United States or removed to a place address unknown will be made to Army Exchange Service for transmittal to such departed organizations.

(6) Disposition of funds due to organization disbanded. When it is determined under (3) above that a distribution should be made to an organization disbanded, the amount due will be set aside to be disposed of in such manner permitted by these

regulations as may be recommended by the exchange council and approved by the commanding officer. If an organization departed prior to disbanding and the amount due is transmitted for payment as provided in (5) above, Army Exchange Service will return the funds to the exchange officer for disposition as provided in this subparagraph.

Section II

Personnel

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15. General.

a. (1) So far as is practicable, exchanges will be operated by civilian employees, with Army officers in executive control.

(2) Great care will be exercised in the selection of personnel in order that an efficient and permanent body of civilian employees may be developed.

b. In exchanges the entire operation is conducted by an exchange officer, and such assistant exchange officers and civilian assistants and enlisted men as authorized in paragraph 21 as may be necessary for the proper conduct of the exchange.

16. Commanding officer. a. The commanding officer, subject to the provisions of paragraph 11 and subject to the administrative control of the

commanding general of the service command, has complete jurisdiction over and is responsible for the conduct of the exchange pertaining to his command.

b. Subject to the provisions of paragraph 11, he will carefully select and appoint the exchange officer who must be fully in sympathy with the purpose of the exchange and possess the business qualifications for its successful operation. For large exchanges a field officer of extensive experience should be selected. Frequent replacement of efficient exchange officers is detrimental to successful operation.

c. He will appoint such assistant exchange officers and detail such enlisted men as may be necessary to conduct the exchange business. See paragraph 21.

d. He will appoint the exchange council as prescribed in paragraph 17a(1).

e. He will appoint officers to take the inventory as prescribed in paragraph 24b, and that inventory taken upon transfer of the exchange from an exchange officer to his successor.

f. He will, when field representatives for auditing purposes are not provided by the commanding general of the service command, appoint a qualified officer to make the audit prescribed in paragraph 26.

g. He will consider and take formal action on the proceedings of the exchange council as recorded in the exchange council book and enter as a remark on the financial statement therein his certificate that the exchange was operated, during the period cov-

ered by the report, in compliance with the annual Military Appropriation Act.

h. In case of his disapproval of the recommendations of the exchange council, he will transmit his comments thereon to the council and, in case of continued disagreement, will submit the proceedings to the commanding general of the service command whose decision in the matter will be final.

i. All contracts involving service, equipment and concessions to be executed by the exchange officer require the approval of the commanding officer prior to the execution. See paragraph 33.

17. Exchange council. a. Organization and procedure.

(1) An exchange council, appointed by the commanding officer, will be established as an advisory body to the exchange officer and the post commander.

(2) The membership of the council, appointed by the commanding officer, will consist of the exchange officer and not more than six officers selected from the command. The commanding officer will not be a member of the council except when there are not more than three officers on duty at the post.

(3) The senior member of the council will preside, unless he is the exchange officer, and the exchange officer will act as recorder at meetings of the council.

(4) The council may delegate to an executive committee of its members any specified portion of its duties, but in such a case the council retains its responsibility.

(5) Each member of the council will have one vote.

(6) The council will meet at such times as may be directed by the commanding officer or requested by the exchange officer.

b. Duties. The duties of the council are to—

(1) Examine the inventorying and auditing officers' reports, ascertain that the inventory and audit have been made in accordance with these regulations, and take cognizance of and recommend action upon any irregularities discovered.

(2) Examine the sources of profits and losses and recommend action in appropriate cases.

(3) Make recommendations regarding all major expenditures other than those for merchandise and expense incident to the usual operation of the exchange.

(4) Recommend amount of remuneration of employees.

(5) Insure that the proceedings of the council are recorded in the council book and that the council book is kept as prescribed in d below.

(6) Recommend appropriations and distributions to organization funds as prescribed in paragraph 14.

(7) Consider the reports of the committee of noncommissioned officers and make recommendations in connection therewith when indicated.

(8) Recommend changes in the policy, organization, or scope of activities of the exchange not inconsistent with the expressed policies of higher authority or these regulations, and to recommend

to the commanding officer the adoption of such policies as will insure sound public relations.

(9) In those cases where superior authority does not prescribe, recommend the articles to be sold and those that are to be discontinued and, with due consideration for the purposes of the exchange stated in paragraph 3, recommend the prices at which such articles will be sold.

(10) Recommend prices to be charged for services or admissions to any of the activities of the exchange, including those of concessionaires.

(11) Make recommendation of action to be taken in all cases where the sales accountability report shows a shortage or overage of more than 1 per cent of the gross sales in any department or activity except manufacturing activities.

(12) Recommend the terms of any rental or installment purchase contract to be entered into by the exchange (par. 12e(4)). See paragraph 33c.

(13) Recommend the amount and terms of repayment of funds to be borrowed from the Army Exchange Service for the purpose of financing new or expansion of established exchanges.

(14) Inquire into compliance with these regulations and recommend action upon any irregularities discovered.

c. Liability of council. See paragraph 8.

d. Council book. The council book will consist of—

(1) The minutes of the meetings, including a formal record of attendance and absentees by name and grade, signed by the presiding officer and re-

corder, with reports of executive committees, when appointed by the council, attached as exhibits.

(2) A record of the action of the commanding officer upon the proceedings and recommendations of the council.

(3) The certificate of inventory officers as provided in paragraph 24a.

(4) The financial statements of the exchange (exhibits A to F, Manual of Uniform System of Accounts), including those made upon transfer of the exchange from one exchange officer to another as prescribed in paragraph 18e(2).

(5) The reports of auditing officers prescribed in paragraph 26g.

18. Exchange officer. a. The exchange officer is in executive control of the exchange. He is responsible for its management and accounting, the performance of duty and discipline of assistants and employees, and is the custodian of its property and funds.

b. He will acquaint himself with the principles of modern accounting and be responsible that the principles of the exchange accounting system are in conformity with these regulations, and with the Manual of Uniform System of Accounts issued by the Army Exchange Service.

c. (1) He will keep exchange funds except as provided in (2) below, in his exclusive personal control either in the exchange or by depositing them as follows:

(a) When practicable, in national bank.

In cases where the working balance of funds is

greater than the amount of the Federal insurance of deposits, appropriate working balances will be fixed by action of the council, approved by the commanding officer. Any funds in excess of appropriate working balances will be—

1. Invested in Government securities in accordance with policies to be promulgated from time to time by the Chief of the Army Exchange Service, or

2. Such cash reserves as may be authorized by duly constituted authority may be deposited in a separate account.

If bank balances exceed the amount of the Federal insurance of deposits it is the responsibility of the exchange officer to require the bank or banks to deposit adequate collateral to secure the safety of such excess.

(b) In State bank, when impracticable to deposit in national bank. Deposits should be made, when possible, in a State bank which is a member of the Federal Deposit Insurance Corporation. The provisions of (a) above will govern except that a State bank may not be required to deposit collateral to secure such excess funds. The exchange officer will therefore be required to secure the cooperation of the bank or banks in arranging for such collateral, if not contrary to the laws of the State in which such bank is chartered.

(2) The exchange officer may, with the approval of the commanding officer, entrust exchange cash

to assistant exchange officers and bonded employees in amounts not greater than minimum requirements for change and petty cash disbursements at branches or departments.

(3) He will be responsible that none of the personnel of an exchange has in his or her possession exchange funds in excess of his or her bond. All funds entrusted to exchange personnel will be recorded in such manner as to permit recovery against the surety in case of loss or default.

(4) He will not permit an accumulation of funds in the exchange office at any time in excess of the requirements of the business or as dictated by the accessibility or limitations of banking facilities. He will apply to the commanding officer for adequate guard to protect any substantial accumulation of funds in the exchange.

(5) He will be in sole control of exchange bank accounts. Authority to make bank transactions other than deposits will not be delegated to any other person unless, after a request by the exchange officer, it is so recommended by the exchange council and approved by the commanding officer.

(6) He will be responsible for the proper taking of inventory by exchange personnel. See paragraph 24a.

(7) Funds of exchanges, although not public moneys within the meaning of sections 5488, 5490 and 5492 of the Revised Statutes, are entrusted to officers of the Army in their official capacity and their misapplication is punishable under the Articles

of War. The loaning of exchange funds is prohibited.

(8) He may, when there is no United States Army disbursing officer readily accessible, cash final statements of discharged enlisted men with exchange funds, retaining a portion sufficient to afford protection against loss due to error until the final statement has been paid by a disbursing officer and then remitting the balance, less any expense of the transaction, to the discharged enlisted men. The exchange assumes no liability for overpayment made by United States Army disbursing officers, this liability resting on the officer who signs the final statements or the United States Army disbursing officer who pays them, according to the source of error.

(9) He may use exchange funds to cash checks, with the authority and under such restrictions as may be recommended by the exchange council and approved by the commanding officer. Any fees or bank charges involved will be paid by the persons for whom the checks are cashed.

(10) He will be responsible that the combination of each safe in the exchange is known only to two persons, other than himself, who will be accountable for the funds safeguarded therein, and that the safe combination is changed when the responsibility for funds is transferred from such persons to other persons. A copy of the combination of each safe will be deposited in a sealed envelope with the post adjutant.

(11) When the necessity or volume of the business of an exchange render such action desirable,

the commanding officer may in his discretion authorize the exchange officer to use a mechanical or electrical check signing machine of a type approved by insurance underwriters, except that the use of such machine will not relieve the officer of any responsibility in the issuance and safeguarding of checks.

d. He will be responsible that the provisions of paragraph 12 are complied with.

e. He will be responsible that, upon his assumption of or relief from the duties of exchange officer, the following procedure is carried out:

(1) If for a temporary period, the exchange officer will be relieved of control of and responsibility for exchange operations, property, and funds for such period beginning with the close of business of the day of transfer to the relieving officer, as shown by memorandum receipt, and ending with the resumption of such control and responsibility at the close of business on the day of return, as shown by memorandum receipt. Such receipts will be recorded in the exchange council book.

(2) If the relief is permanent, an inventory as prescribed in paragraphs 16e and 24 will be made supporting a statement of assets and liabilities certified by the officer relieved to be complete, true and correct to the best of his knowledge and belief and signed as a receipt by the relieving officer. The signed statement forms a part of the council books as prescribed in paragraph 17d(4).

f. He will make sure that no concessionaire of the exchange represents himself to the public as the agent of the exchange by the use of the words "—Exchange" in the title of his business or in any other manner.

g. He will enforce upon concessionaires the limitations imposed by these regulations.

h. He will be responsible that no officer charged with any duty in connection with the exchange receives any extra remuneration therefor and that no officer or employee accepts or receives any gift, privilege, or perquisite from the exchange or from vendors or vendees of the exchange.

i. He is, within the specific authority vested in him by these regulations, empowered to execute contracts in the name of the exchange.

j. He will, with regard to recommendations of the council and in conformity to applicable Government regulations, employ and fix the pay of civilian employees of the exchange.

k. He will, upon assuming the duty of exchange officer, carefully ascertain the number of each denomination of unissued coupon books on hand and thereafter insure that a record is kept of receipts and issues of such books to agents of the exchange who make sales direct to enlisted patrons.

l. He will be the custodian of redeemed coupons turned in with the manager's daily report and, the count having been verified, he or an assistant exchange officer will personally witness the destruction of all coupons so received.

m. He will see that the accounting system is

maintained and operations conducted in such a manner as to provide adequate measures for the control of losses through dishonesty of employees or customers.

n. He will make certain that all of the incoming first-class mail for the exchange is received and opened by him personally or by an assistant exchange officer or other designated and responsible person.

o. The exchange officer may delegate to an assistant exchange officer any or all the duties of the exchange officer except in cases where laws and regulations make the performance of the duty mandatory on the part of the exchange officer.

p. The exchange officer will be financially liable for losses of exchange funds and property where the loss was by reason of his negligence or dishonesty. See paragraph 8.

19. Assistant exchange officer. Assistant exchange officers perform such duties as may be prescribed by the exchange officer.

20. Exchange office manager. a. The exchange office manager is a civilian assistant of the exchange officer.

b. In the informal absence of the exchange officer and assistant exchange officers, he is in immediate control of the exchange and may act for them in accordance with the policies of the exchange officer. In such cases the exchange officer retains responsibility for the actions of the manager.

c. The manager's duties, to be performed in small exchanges by himself or, in large exchanges,

under his supervision and responsibility, are as follows:

(1) He will keep the books and records of the exchange except those prescribed to be kept by the exchange officer.

(2) He will make such spot checks and verifications of the exchange accounting, coupon books, etc., as will insure accuracy and fidelity on the part of his subordinates in the exchange.

(3) He will keep the stock and sales accountability records except where he personally is the custodian of the stock room or sales room. See paragraph 23c.

(4) He will be responsible and account for the coupon books turned over to him by the exchange officer.

(5) He will collect, safeguard, and turn over to the exchange officer daily the cash and coupons received for sales and the receipts for petty cash disbursements.

(6) (a) He will prepare and submit to the exchange officer a manager's daily report (see Manual of Uniform System of Accounts).

(b) In large exchanges where assistant managers or other employees perform part of the duties of the manager either in charge of branches or as cashiers, etc., each of them will make a daily report of his transactions, which may, if desired, be consolidated into one daily report covering all activities (see Manual of Uniform System of Accounts).

(c) The data in the manager's report will

be verified and initialed by custodians of departments, certified correct by the manager, examined and approved by the exchange officer or assistant exchange officer, and permanently filed in chronological order.

(7) He may make purchases of merchandise as provided in paragraph 12a.

21. Enlisted employees. a. The commanding officer of the post, camp, station or installation may, subject to the approval of the commanding general of the service command, authorize the use of enlisted men in exchanges.

b. Position responsibility of enlisted employees will be as prescribed for civilian personnel.

c. The wage of an enlisted employee will not exceed one-half of his base pay exclusive of allowances or other increase unless otherwise determined by the commanding general of the service command.

d. The employment of enlisted men by exchange concessionaires is prohibited.

e. The commanding officer of tactical troops not located on military reservations is authorized to use enlisted men in the operation of the exchange without obtaining approval of the commanding general of the service command.

Section III

Operations

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22. Accounting and bookkeeping. a. This phase of exchange operations is covered in a separate publication entitled "Manual of Uniform System of Accounts, Forms and Accounting Procedure for Post, Camp, Station and Field Exchanges," in which detailed bookkeeping, accounting, auditing, financial statement, and supplementary forms are provided.

b. All exchanges will install the system prescribed therein. The small exchange, which does not have a warehouse, may use only that part of the system which is applicable as indicated in section VII thereof or as otherwise provided for by the Army Exchange Service.

c. In exceptional cases, the Chief of Army Exchange Service may permit, in writing, deviation from a and b above.

d. All transactions will be recorded and posted currently so that periodic audits, statements and reports can be made without delay.

e. (1) Copies of such financial or other reports as the Chief of Army Exchange Service may direct will be forwarded promptly to the commanding general of the service command and to the Army Exchange Service, War Department.

(2) The remittance of the prescribed percentage of the gross sales payable to the "Army Exchange Fund" as provided in paragraph 11c will be forwarded monthly to the Chief of Army Exchange Service.

(3) The Exchange Branch of the service command headquarters will consolidate and forward such reports to the Army Exchange Service as from time to time directed by the Chief of Army Exchange Service.

f. Consistent with the volume of business, use should be made of efficient business machines purchased from exchange funds.

g. Destruction of old records. All invoices, canceled checks, papers, and books relating to the business of an exchange, except the exchange council book, and pertaining to accounts that have been closed more than 3 years, may be destroyed as no longer required for the protection of the exchange, except in the case of an exchange where the statute of limitations prescribes a longer period on such accounts, in which case the papers will be kept for such longer period, unless with respect to an entry or omission of an entry therein a civil claim or criminal action shall have been presented or initiated, under which circumstances the destruction of the records concerned will be postponed until

after final disposition of the claim or criminal action. Under the direction of the commanding officer, the papers specified will be destroyed by the exchange officer who will record the action in the exchange council book.

h. Disposition of records when post is abandoned. In the event of the abandonment of a post, camp, station or installation, the exchange council book, together with all records not destroyed as above provided, will be forwarded to the commanding general of the service command for appropriate disposition.

23. Stock records and sales accountability. a. A form of stock record and detailed procedure in the operation thereof are described in the Manual of Uniform System of Accounts. No deviation in principle will be permitted.

b. (1) In small exchanges merchandise may be charged direct at selling prices to the sales accountability record, placed immediately in stock, and accounted for on the inventory.

(2) A form of sales accountability record and detailed procedure in the operation thereof are described in the Manual of Uniform System of Accounts. No deviation in principle will be permitted.

c. In order that responsibility for shortages developed by stock or sales accountability records may be definitely placed, it is necessary that separate accountability be set up for each department or subdivision for which a control is required. In no case will the custodian keep his own accountability or make entries therein except for his own information. In small exchanges conducted by an

exchange officer and a manager, the exchange officer will keep the accountability record.

d. Accountability for manufacturing activities such as restaurants, meat markets, etc., where the merchandise received loses its identity, before sale is not authorized.

24. Inventory. a. The Chief of Army Exchange Service will prescribe the procedure for and frequency of inventories. When an inventory is taken it is the direct responsibility of the exchange officer and employees of the exchange, particularly those charged with stock or sales accountability, that the assets are inventoried for the inventory officer. It is the responsibility of the inventory officer to make a sufficient recheck of the inventory so he can certify that it is correct to the best of his knowledge and belief.

b. The inventory officer and assistants appointed under paragraph 16e will, at a designated time, make a recheck of the inventory of the exchange, to include merchandise, fixtures, equipment, general supplies, containers and unissued coupon books.

25. Commanding general of service command—Specific duties. a. See paragraphs 4, 7, 9, 10, 11, 14, 16, 21, 22, 26, 27, 28, 33 and 34.

b. The commanding general of the service command, as provided in AR 170-10, is charged with—

(1) General supervision of exchange operations and management. The commanding general of the service command may take appropriate action on any matter pertaining to an exchange investigated and reported upon.

(2) Auditing the accounts of exchanges.

26. Auditing. a. A balance sheet audit will be made of each exchange not less frequently than quarterly. Where conditions of operation and management make it advisable, more frequent audits will be made. The commanding general of the service command will be responsible that all such audits are made.

b. Annual or more frequent unannounced examinations of each exchange will be made as directed by the commanding general of the service command.

c. A qualified field representative officer will be provided by the commanding general of the service command to perform the audit. When this is not possible and the commanding officer so notified, a qualified officer will be detailed by the commanding officer as provided in paragraph 16f.

d. (1) The procedure outlined in the Manual of Uniform System of Accounts will serve as a guide for auditing. It is the responsibility of the auditing officer that he develops by it sufficient assurance to enable him to certify as required in g(10) below.

(2) The auditing officers need not be limited by the procedure outlined in the Manual of Uniform System of Accounts or other prescribed procedures. Any matter pertaining to the exchange may be investigated and reported upon, together with recommendations in connection therewith.

e. (1) Upon the completion of the financial statements by the exchange, the auditing officer will make a balance sheet audit for the period since the

previous audit or longer period, if so directed by the commanding general of the service command.

(2) In making a balance sheet audit, the auditor will verify the assets and liabilities of the exchange, including a test check of income and expense items, ascertain whether the accounting procedures are correct and in compliance with regulations and whether the financial statements (exhibits A to F, Manual of Uniform System of Accounts) are in agreement therewith.

f. (1) Upon the request of the commanding officer and with the approval of the commanding general of the service command, the auditing officer will make a detailed audit for the period since the previous audit or longer period, as directed by the commanding general of the service command.

(2) In making a detailed audit, the auditing officer will assume complete control of the exchange and its activities and, in addition to the procedure described in a(2) above, will make examination and verification from original sources of all entries in the accounting records for the audit period; verify the status of accounts by means of confirmation letters mailed to debtors and creditors; and recommend a reappraisal of assets where indicated.

g. Upon completion of the audit, the auditing officer will prepare a report to the commanding officer of the post, camp, station or installation at which the exchange is located, a copy of which will be forwarded by the auditing officer to the commanding general of the service command, to include—

(1) Authority, type of audit made, and the period covered by the report.

(2) Scope of the audit.

(3) Qualifying comments on items appearing on the financial statements.

(4) Comparison of the result of operations of the period under review with the preceding period.

(5) Statement of the amount of funds available for distribution, taking into consideration the amount of profit accrued since the last distribution.

(6) List any department whose accountability overages and/or shortages exceed 1 per cent of such department's gross sales and recommendations as to the action to be taken.

(7) List of delinquent accounts receivable as of the date of audit.

(8) Statement of insurance coverage, showing the type of coverage and the amounts in total or limit for each type, together with a statement as to the adequacy of the coverage in conformance with paragraph 31.

(9) General comments and recommendations.

(10) Certificate: "I/we hereby certify that in my/our opinion, subject to the foregoing comments, the statements herein contained correctly state the financial condition of the Exchange on, and the results from operations for the period from to, inclusive."

(11) Financial statements, exhibits A to F, inclusive, (Manual of Uniform System of Accounts).

h. Where public accountants are employed to audit, the report above prescribed will be amended to the effect that the auditing officer has, with their

assistance (stating the name of auditing firm), made the required audit.

27. Civilian auditors. Under unusual circumstances and only after approval by the commanding general of the service command the commanding officer may authorize the employment of a qualified civilian accounting firm at stated intervals to audit the accounts of the exchange at its expense. In such cases the commanding officer, the exchange council, and the auditing officer retain their full responsibility. The officer designated as the auditing officer may work with the accountant, in which case he is authorized to amend the certificate required of him as indicated in paragraph 26h.

28. Boards of officers. Boards of not less than three disinterested officers will be appointed by the commanding officer to investigate and report upon losses sustained by an exchange where any question of personal liability or responsibility is involved. Boards making such investigations will include in their reports their opinions as to responsibility for the loss and recommendations as to appropriate action for decision of the commanding general of the service command.

29. Committee of noncommissioned officers. a. To insure adequate consideration of the interests of enlisted personnel, the commanding officer will appoint a committee of noncommissioned officers for the entire command to be not less than three nor more than six in number.

b. This committee will meet at the call of the commanding officer at least once in each quarter and oftener, if he desires. The committee will submit

to the commanding officer, either orally or in writing, views of the enlisted personnel concerning desirable changes in or addition to internal operations of the exchange. Such views will be transmitted by the commanding officer to the exchange council and recorded in the council book, together with such action as the commanding officer may direct in connection therewith.

30. Losses. As to losses caused by negligence or mismanagement, see paragraph 18p.

31. Insurance. a. General. Exchanges will procure adequate insurance coverage against types of losses and liabilities as prescribed from time to time by the Chief of Army Exchange Service.

b. Surety bonds. The exchange officer, assistant exchange officers, and each employee, including the exchange office manager, who is entrusted with the custody of any money or property of the exchange or accountability therefor, such as warehouse managers, storekeepers, clerks, branch managers, cashiers, and bookkeepers will be bonded by a reputable bonding company as surety, at the expense of the exchange, in an amount that will protect the exchange from loss in case of defalcation. Limitations which may be imposed by other Army Regulations on the amount of bonds covering accountable officers and employees will not be applicable to exchange officers or personnel. Coverage will be written under a Position Schedule form of bond, unless the number of positions bonded justifies the purchase of a Blanket Position bond at a lower premium.

c. Policies covering liability insurance will con-

tain a stipulation, or rider, to the following effect:

The company agrees that the fact that the insured is a Government instrumentality will not be interposed as a defense in any lawsuit in which the company's liability under this policy is in any way concerned, unless so requested in writing by the insured.

In no case will such defense be requested of the company by an exchange unless and until it has been specifically authorized to do so by the War Department.

d. Accounting and asset inventory records of the exchange will be kept closely up to date and in proper form to facilitate the settlement of insurance claims.

e. Group insurance for civilians. Expenditure of exchange funds is authorized for the payment of the employer's portion of the cost of a contributory group insurance plan for civilian employees.

32. Taxes. a. Federal taxes.

(1) Exchanges are Government instrumentalities expressly recognized by Congress in annual appropriation acts and by the courts. Since it has never been the general policy of the Government to tax its own enterprises or its own manner of conducting business, exchanges are exempt from the payment of Federal income taxes, of excise taxes on furs, cosmetics and jewelry. Exchanges are also exempt from the payment of Social Security Taxes.

(2) Exchanges within the purview of the Reve-

nue Act of 1914 (38 Stat. 716) are subject to the stamp taxes imposed by that act. Accordingly such exchanges are not permitted to sell merchandise on which special Federal stamp taxes are required until such stamps have been affixed. See JAG 012.2, April 8, 1913.

(3) Federal manufacturers excise taxes are payable by the exchange on merchandise purchased for resale. Merchandise for use of exchanges and not for resale is exempt. In the latter case the use of tax exemption certificates are authorized.

b. State taxes.

(1) Consent has been given by the Federal Government to the imposition of State gasoline taxes on sales by exchanges for use in vehicles other than United States Government-owned or used vehicles. Army exchange vehicles being used for a governmental function are entitled to all the rights and exemptions of government-owned vehicles and gasoline used in exchange vehicles is exempt from the payment of such tax to the State. In general, no sales, income or property taxes of any nature, or occupational taxes, direct or indirect, are payable by exchanges to any State, or subdivision thereof, or territorial government.

(2) Questions as to whether any taxes noted in (1) above are payable which arise within the geographical limits of a service command, department, or foreign government, will be forwarded to the commanding general of the service command for decision. The commanding general of the service command may, when necessary, forward any such

question to the Chief of Army Exchange Service accompanied by the opinion of the judge advocate of such service command. The Chief of Army Exchange Service will determine such questions or, if he deems it necessary, forward the question to the Judge Advocate General for decision. In no event will a ruling by State, territorial, or local authority that such a tax is payable be acted upon without reference as hereinabove directed.

c. Social Security Act.

(1) The Commissioner of Internal Revenue in a letter dated September 29, 1942, ruled that services performed "in connection with the operation of Army exchanges are excepted from 'employment' by reason of the provisions of paragraphs (6) of Sections 1426 (b) and 1607 (c) of the Federal Insurance Contributions Act and the Federal Unemployment Tax Act, respectively. Accordingly, the Federal employment taxes are not applicable with respect to such services."

(2) The ruling of the Commissioner of Internal Revenue is considered applicable to State as well as Federal taxes. Therefore, exchanges will not pay or collect Federal or State taxes attempted to be imposed under the authority of Federal or State employment or Social Security acts.

33. Contracts. a. Under the provisions of these regulations the exchange officer is the contracting officer for the exchange, and he is authorized to execute a contract obligating the exchange.

b. All contracts and agreements to which exchanges are parties will contain when applicable the

statement that such contracts will be terminated when an exchange is liquidated or for other reasons at the option of the exchange.

c. Contracts on behalf of an exchange will not cover periods of more than 1 year without the approval of the commanding general of the service command.

d. Proposed concession contracts will be submitted to the commanding general of the service command for approval, as provided in paragraph 10c.

e. All contracts involving future performance will be reduced to writing, signed by the contracting parties, and filed in the records of the exchange.

f. All contracts that involve the use of Government property not under the control of the exchange will be submitted to the commanding general of the service command for approval.

g. Contracts involving the sale of 3.2 per cent beer entered into in connection with the provisions of paragraph 10b(7) of these regulations will, without exception, be accompanied by affidavit of the manufacturer and distributor of such beer certifying that the alcoholic content of such product does not exceed that permitted by these regulations.

h. (1) Exchange contracts are solely the obligation of the exchange. They are not Government contracts and the distinction between exchange contracts and Government contracts will be observed and clearly indicated at all times.

(2) Contracts for the erection of temporary exchange buildings will contain a statement that the

proposed construction is an exchange transaction and that the exchange alone is responsible for the debt, and not the Government.

i. When applicable, contracts for the erection of temporary buildings will contain a statement that immediately upon completion of the building, title thereto passes to the exchange. See paragraph 9c(5).

j. Notwithstanding the provisions of a above and paragraph 18i, whenever an exchange outside the continental limits of the United States makes purchases within the United States as provided in paragraph 12a(6) the fiscal officer appointed for such exchange is, within the scope of his assigned duties under such appointment, the contracting officer for the said exchange in limitation of the functions of the commanding officer and the exchange officer as set forth in a above and paragraph 16i.

34. Use of Government vehicles. The use of Government vehicles for exchanges may be authorized by the post commander or the commanding general of the service command in appropriate cases as provided in paragraph 7b(4) AR 850-15.

35. Loans. Funds for establishment, expansion, or other purposes in the operation of exchanges may be obtained by loan from Army Exchange Service. Exchanges will not borrow money from other sources except with permission of the Chief of Army Exchange Service.

Section IV

Miscellaneous

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36. Posting of selling prices. Price lists will be posted conspicuously in all activities of exchanges, including those of concessionaires, and articles stocked for sale will be conspicuously priced.

37. Posting of financial statement. A copy of the current financial statement and a statement of operations will be exhibited in a conspicuous place in one of the rooms of the exchange during the ensuing accounting period.

38. Correspondence channels. Correspondence on matters pertaining to exchanges, originating from any exchange, will be forwarded to the commanding general of the service command for appropriate action. Where an expression of higher authority is mandatory or is desired prior to the taking of appropriate action, the commanding general of the service command will forward the matter,

together with his recommendations, to the Chief of Army Exchange Service for appropriate action.

39. Advice of finance officers. Locally available officers of the Finance Department may be consulted on the financial conduct of exchanges.

40. United States Attorney; services and advice of. An exchange officer is entitled to the legal advice or services of the local United States Attorney to protect the rights and interests of the exchange. (Ops. JAG, September 8, 1919). See AR 410-5. If the matter is not urgent, the views of the commanding general of the service command should be obtained before seeking such advice.

41. Penalty envelopes. Exchanges may use penalty envelopes only for proper correspondence pertaining to their business but not for the transmission of merchandise or solicitation of customers.

42. War Department communication system. Messages on exchange business may be transmitted without charge over telegraph, radio, and cable lines owned and operated by the War Department, the exchange being liable for charges on connecting lines.

43. Operation of canteens for civilian enemy aliens and prisoners of war. Notwithstanding the provisions of any other paragraph of these regulations, Army exchanges are authorized to operate canteens for interned civilian enemy aliens and prisoners of war. Such canteens will be operated in accordance with the regulations of the Provost Marshal General and such procedure not inconsistent therewith as may be prescribed from time to

time by agreement between Provost Marshal General and the Chief of the Army Exchange Service.

44. Publications using words "Army exchanges," etc. Exchange officers and exchange personnel will not be connected in any capacity with any publication published by a private individual, partnership, corporation, or association of any type using as or in its title or name the words "Army exchange," "Post exchange," or similar words by which it may be inferred that the publication is sponsored or approved by Army Exchange Service. No such publication will be circulated or distributed in any area under the jurisdiction of the War Department unless it has printed therein in a prominent place a statement as follows:

This periodical is not published by nor is it an official publication of Army Exchange Service or of the War Department.

(A. G. 331.36 (2-15-43)).

By order of the Secretary of War:

G. C. MARSHALL,
Chief of Staff.

Official:

J. A. ULIO,
Major General,
The Adjutant General.

Distribution:

A;E.

Sup. Ct. #2631.

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In the Circuit Court of the First Judicial Circuit
Territory of Hawaii

L. No. 17365

At Term In Law

THOMAS H. BRODHEAD,
d.b.a. T. H. Brodhead Co.,

Plaintiff,

vs.

WILLIAM BORTHWICK, Tax Commissioner and
Tax Collector,

Defendant.

Action to Recover Gross Income Taxes
Paid Under Protest

DECISION

This in an action brought under the provisions of Section 1575, Revised Laws of Hawaii 1945 (formerly Section 571, Revised Laws of Hawaii 1935) to recover general excise taxes (sometimes called gross income taxes) assessed under the provisions of Act 141 (Ser. A-44) Session Laws of Hawaii 1935, as amended. Said tax law hereinafter is referred to as the General Excise Tax Law.

Plaintiff seeks to recover said taxes on the ground that the same were wrongfully and illegally demanded and collected, for the reason that of the amount of \$695,062.72 claimed by defendant as the additional amount taxable at the rate of 1½%, \$691,777.66 thereof represents sales to the United States post exchanges and ships' service stores, and the amount of \$3,285.06 represents sales to the United

States or other instrumentalities, departments, or agencies of the United States, which [30] amounts were claimed to be exempt from gross income tax under the provisions of the General Excise Tax Law.

In the second place, it was claimed that the imposition of such taxes was in violation of Article I, Section 8, Clauses 12 and 13, and the Fifth Amendment of the Constitution of the United States, and of Section 55 of the Hawaiian Organic Act.

Finally, it was claimed that in no event can the gross income tax from sales to post exchanges and ships' service stores and other instrumentalities or agencies of the United States be taxed at more than $\frac{1}{4}$ of 1% when such sales to said agencies or instrumentalities are made for resale.

The case was tried jury waived before the Fifth Judge of this court, commencing July 6, 1944. Decision and judgment were rendered for the plaintiff and the defendant brought the case to the Supreme Court by writ of error. On March 4, 1946, the Supreme Court rendered its opinion reversing the judgment appealed from and directing that the cause be remanded for a new trial. A petition for rehearing was denied March 27, 1946.

In the Supreme Court this cause was consolidated for briefing and argument with Law. No. 16956, involving taxes paid during a period prior in time to the period involved in this case. Said action also was remanded for new trial, but the parties have stipulated that said Law No. 16956 may be held for trial awaiting the final disposition of this case.

The case again came on for trial jury waived on May 8, 1946. Most of the facts have been stipulated

by the parties. It further was stipulated that all of the evidence received upon the trial of Law. No. 16956 on June 16, 1943, should be deemed applicable to this case and considered with the same effect as if received in this case; this brings into the record in this case the testimony of Mortimer J. Glueck and Torkel Westly, and defendant's Exhibit 1, which is an advertisement entitled "Notice to Gross Income Taxpayers." Also made a part of the record by stipulation of the parties are Exhibit A, which is plaintiff's protest filed at the time of payment of the taxes which plaintiff seeks to recover, Exhibits B and C, which are copies of plaintiff's amended tax returns and the Tax Commissioner's assessments, and Exhibit D, a copy of the Post Exchange Regulations as revised March 19, 1943.

On the foregoing record the court hereby makes the following findings of fact and conclusions of law:

Findings of Fact

1. Plaintiff is and at all times hereinafter mentioned was a resident of Honolulu, City and County of Honolulu, Territory of Hawaii; plaintiff is the general partner of a registered special partnership doing business in Honolulu aforesaid under the firm name and style of T. H. Brodhead Co. Said special partnership was organized on or about October 1, 1942, under and pursuant to Sections 6870 to 6892 inclusive of Chapter 225 of the Revised Laws of Hawaii 1935, and was in existence at the time of repeal of said sections by Act 162, Session Laws of Hawaii 1943.

2. Defendant is and was at all relevant times [32] the duly appointed, qualified and acting Tax Com-

missioner of the Territory of Hawaii, and as such is and was at all relevant times in charge of the administration and enforcement of Act 141 (Ser. A-44) of the Session Laws of Hawaii 1935, as amended from time to time, and with respect to any money representing a claim of the Territory for taxes pursuant to said General Excise Tax Law (hereafter referred to as gross income taxes) was a public accountant of the Territory within the meaning of Section 1575 of the Revised Laws of Hawaii 1945.

3. Plaintiff made monthly gross income tax returns for each of the months of October, 1942, to March, 1944, inclusive, and annual returns of gross income tax for each of the years 1942 and 1943, at the times required by law; plaintiff duly paid the gross income tax on the amounts of gross income reported in said returns as taxable, as and when the same was due and payable. On April 26, 1944, plaintiff, with the permission of the Tax Commissioner, filed amended returns covering the periods of October 1 to December 31, 1942, January 1 to December 31, 1943, and January, February and March, 1944.

4. On May 2, 1944, the Tax Commissioner issued first notices of proposed additional assessments of gross income taxes for the aforesaid periods, increasing the gross income taxable and the tax thereon, in the amount of \$10,425.95.

5. On May 15, 1944, the plaintiff waived the necessity of a thirty day interval between the first and second notices of assessment, without prejudice to his claims, and the proposed additional assessments were made. [33] On the same day, May 15, 1944, plaintiff paid under protest the sum of \$10,-

425.95 so assessed, a true copy of plaintiff's protest being annexed to the complaint as Exhibit A.

6. Plaintiff made sales to the United States government and its post exchanges and ships' service stores in the respective amounts and for the periods below set forth, and no gross income tax has been paid with respect thereto except the tax so paid under protest. Such sales were reported by plaintiff but the income therefrom was claimed to be exempt as derived from sales to the United States government and its post exchanges and ships' service stores; moreover, plaintiff classified the sales to the post exchanges and ships' service stores as "wholesaling." The following is a summary of the sales involved, showing the taxes assessed, and the claims made by the plaintiff.

Item No.	Amount of Gross Income and Period	Source*	Rate of Tax Assessed, and Amount of Tax Paid Under Protest	How Returned by Plaintiff
1.	\$130,985.93 Oct.-Dec., '42	PX sales	1½% \$1,964.79	Wholesaling; exemption claimed.
2.	\$ 2,120.40 Oct.-Dec., '42	Sales to U.S.	1½% \$ 31.81	Retailing; exemption claimed.
3.	\$115,106.05 Jan.-April, '43	PX sales	1½% \$1,726.59	Wholesaling; exemption claimed.
4.	\$ 169.92 Jan.-April, '43	Sales to U.S.	1½% \$ 2.55	Retailing; exemption claimed.
5.	\$331,205.04 May-Dec., '43	PX sales	1½% \$4,968.08	Wholesaling; exemption claimed.
6.	\$ 270.75 May-Dec., '43	Sales to U.S.	1½% \$ 4.06	Retailing; exemption claimed.
7.	\$114,480.64 Jan.-Mar., '44	PX sales	1½% \$1,717.21	Wholesaling; exemption claimed.
8.	\$ 723.99 Jan.-Mar., '44	Sales to U.S.	1½% \$ 10.86	Retailing; exemption claimed.

*PX refers to sales to post exchanges and ships' service stores.

7. The post exchanges to which reference is made in this decision are operated under army regulations, a copy of such regulations as revised March 19, 1943, being annexed to the stipulation of the parties as Exhibit D with the same effect as if admitted in evidence; it is hereby found that the army regulations in effect during the period involved in this case were the same in all material respects as said Exhibit D. Such post exchanges do not differ materially from the post exchanges involved in *Standard Oil Co. v. Johnson*, 316 U. S. 481, 86 L. Ed. 1611, June 1, 1942.

8. At no time did any of said post exchanges have a license under the General Excise Tax Law of the Territory, Act 141 (Ser. A-44) of the Session Laws of Hawaii 1935, as amended, and at no time did any of said post exchanges pay any tax under said law.

9. The ships' service stores, to which reference is made in this decision, have the same relation to the United States Navy as the post exchanges have to the United States Army and there is no material difference in the facts with respect to such ships' service stores.

10. Throughout the period involved in this case the gross proceeds of sales made to post exchanges and ships' service stores were assessed by the Tax Commissioner at the same rate of tax ($1\frac{1}{2}\%$) as was applied by him upon the gross proceeds of sales to the War Department or Navy Department or other government departments, irrespective of what was done with the goods after purchase thereof; this likewise was the same rate of tax as was applied upon the gross income from construction contracts

made with the government, including the reimbursement of costs of a cost-plus contractor.

11. In instances in which sales are made to purchasers other than post exchanges and ships' service stores, classified by the Tax Commissioner as not subject to tax under the General Excise Tax Law, he has assessed the tax at the rate of $1\frac{1}{2}\%$ (except when such rate was $1\frac{1}{4}\%$), even though the goods were sold for resale by the purchaser. Such practice was followed throughout the period in question.

Conclusions of Law

A. The General Excise Tax Law of the Territory (Act 141 (Series A-44) Session Laws of Hawaii 1935, as amended) imposes a tax, and throughout the period in question did impose a tax, upon the business of selling tangible personal property in the Territory.

B. Throughout the period in question said tax applied to the plaintiff with respect to the business of selling tangible personal property, including all sales made to the United States government, its departments and agencies.

C. Section 3 of said law did not exempt the plaintiff from tax on the gross proceeds of the sales covered by finding number 6, made by him to the United States government and its post exchanges and ships' service stores.

D. The tax so imposed was and is a tax upon the plaintiff, and does not levy a burden upon or interfere with federal activities. [36]

E. Such tax has only an economic effect upon the United States government, its departments and agen-

cies. Such economic effect is indirect, and does not constitute the tax an invalid burden upon or interference with federal activities.

F. The imposition of said tax was and is within the power of the legislature of the Territory under Section 55 of the Hawaiian Organic Act, and not in violation of Article I, Section 8, Clause 12 or 13 or the Fifth Amendment of the Constitution of the United States.

G. The tax imposed by said General Excise Tax Law upon the business of selling, was and is measured by the gross proceeds of sales of the business. The rate of tax is and throughout the period was as follows:

(1) Upon all gross proceeds of sales to the territorial and federal governments and agencies thereof, charitable institutions, hospitals, fraternal benefit societies, public utilities, users and consumers, and others not subject to general excise tax, $11\frac{1}{2}\%$ (except during certain periods not involved in this case when such rate of tax was $11\frac{1}{4}\%$) this $11\frac{1}{2}\%$ rate being applicable irrespective of whether the goods were sold in wholesale lots or at wholesale prices, and irrespective of whether such goods were intended to be and were resold by the purchasers, or what was done with such goods.

(2) Upon gross proceeds of sales to (a) a licensed retail merchant or jobber for purposes of [37] resale, (b) a licensed manufacturer for incorporation into a product for sale, (c) a

licensed contractor for incorporation into the project required by the contract: $\frac{1}{4}$ of 1%.

H. Said tax law required the Tax Commissioner to and he did include the sales in question with the sales in class (1) above.

I. Post exchanges and ships' service stores are not "merchants" within the meaning of the tax law; on the contrary they are arms of the federal government engaged in performing governmental functions as integral parts of the War Department.

J. Post exchanges and ships' service stores are not "licensed" within the meaning of the tax law, since not required to have and not having a license under section 21 of said tax law.

K. The classifications made by the legislature are natural and reasonable and not discriminatory against the plaintiff or the federal government or its instrumentalities, such classifications being based upon the difference between class (2) sales of goods, which in normal distribution through commercial channels bear two taxes (viz., one when sold at wholesale when the rate is $\frac{1}{4}$ of 1% and one when sold at retail when the rate is $1\frac{1}{2}\%$), and class (1) sales of goods which do not bear two taxes.

L. The Tax Commissioner applied the tax law in this case in conformity with the court's construction of said law, and hence there is no question of administrative discrimination involved in this case. [38]

M. The court hereby adopts as reasons for this decision the reasons stated in the opinion of the Supreme Court rendered March 4, 1946, and the opinion denying rehearing on March 27, 1946.

N. The plaintiff is not entitled to recover the money paid under protest, and the defendant is entitled to judgment dismissing the action.

Let judgment be entered accordingly.

Dated at Honolulu, T. H., this 15th day of May, 1946.

[Seal] /s/ A. M. CHRISTY,
Judge of the Above Entitled
Court.

[Endorsed]: Filed May 15, 1946.

In the Circuit Court of the First Judicial District,
Territory of Hawaii

L. No. 17365

At Term—In Law

THOMAS H. BRODHEAD, d.b.a. T. H. BROD-
HEAD CO.,

Plaintiff,

vs.

WILLIAM BORTHWICK, Tax Commissioner and
Tax Collector,

Defendant.

Action To Recover Gross Income
Taxes Paid Under Protest

JUDGMENT

The above-entitled cause having come on to be heard and the court having rendered its decision on the 15th day of May, 1946, in favor of the defendant, now therefore,

It Is Hereby Ordered, Adjudged and Decreed that the plaintiff take nothing by his complaint and that said action be and it hereby is dismissed.

Dated at Honolulu, T. H., this 15th day of May, 1946.

[Seal] /s/ WILLIAM C. ING,
Clerk of the Above Entitled
Court.

Approved:
 /s/ A. M. CRISTY,
Second Judge, First Circuit
Court, Territory of Hawaii.

Approved as to Form:
 SMITH, WILD, BEEBE &
 CADES.

By /s/ MILTON CADES,
Attorneys for the Plaintiff.

[Endorsed]: Filed May 15, 1946. [41]

[Title of Circuit Court and Cause.]

TRANSCRIPT

Of proceedings had on May 8th and 15th, 1946, before the Hon. A. M. Cristy, Circuit Judge.

Appearances:

For Plaintiff: Milton Cades, Esq., of the law firm of Smith, Wild, Beebe & Cades.

For Defendant: Miss Rhoda Lewis, Assistant Attorney General of the Territory of Hawaii. [42]

May 8, 1946—9:00 A.M.

Miss Lewis: If the Court please, I think it would clarify the record if it were mentioned that that Supreme Court opinion which was the opinion of March 4th, 1946, covered not only the case which I'm trying today but also Law No. 16956 covering an earlier period, but counsel have agreed to proceed with this case and let the other one stand meanwhile. Is that correct, Mr. Cades?

Mr. Cades: That is correct. It seemed simpler to proceed with the one case rather than two. In that connection, the order of consolidation was only for argument in the Supreme Court and it was not a consolidation of causes as such.

The Court: All right. So this concerns additional assessment for 1942, and is that all?

Mr. Cades: No, I believe it covers 1943 only; I don't believe it started with 1942, I believe it started in 1943.

The Court: Well, according to this file I have here in Law No. 17565—is that the one you're trying?

Miss Lewis: Yes.

Mr. Cades: It begins with October, 1942.

Miss Lewis: Yes, that's correct.

Mr. Cades: And continued through March, 1944.

The Court: Yes, according to the tables in paragraph four of the complaint.

Mr. Cades: That's correct, your Honor. Now, I believe it's fair to say that counsel are in agreement pretty much as to methods of shortening the trial, but we are confronted with certain practical problems as far as the record is concerned. The

case before was tried on stipulations which we would like to make a part of this record, together [43] with certain evidence and certain exhibits that were offered in connection with the evidence.

The Court: Well, now, let's identify the stipulations you refer to. In the record on page 20 of the court docket here I find a stipulation filed in open court July 6th, 1944.

Miss Lewis: That is dated June 24th, 1944.

The Court: Well, I just wanted to check up; on this it's dated June 24th, 1944. Is that one of the stipulations to which you refer?

Miss Lewis: Yes.

Mr. Cades: Yes, that's right, to which is attached tax return and copies of assessment notices and Army regulations.

The Court: Yes.

Mr. Cades: Now, then, counsel agree that that be offered in this case as a stipulation in this cause; is that correct?

Miss Lewis: That is correct; it was in this action and it is still in effect a stipulation for this new trial.

The Court: Let the record so show that the stipulation as on file here is part of this particular hearing, as part of the evidence.

Mr. Cades: Yes. Now, then, the next matter is the matter of the transcript of evidence that was adduced in the other case, being Law No. 16956; that we could get from the Supreme Court; that's the transcript of the evidence that was——

The Court (Interrupting): What's the number of the transcript?

Mr. Cades: Law No. 16956.

Miss Lewis: That is covered by paragraph eight of that stipulation. [44]

The Court: 16956?

Mr. Cades: That's right, your Honor.

The Court: Yes.

Mr. Cades: And that's in the record of the consolidated cases in the Supreme Court; I believe that we could obtain the original transcript from the Supreme Court and make that a part of this record.

The Court: Let's incorporate it by reference in the stipulation.

Miss Lewis: Yes.

Mr. Cades: That's correct.

Miss Lewis: Together with the exhibits.

Mr. Cades: Together with the exhibits referred to in the transcript. Is there any more?

Miss Lewis: I think we had one other matter we were willing to stipulate on that was as to the status of the plaintiff in this case, Thomas H. Brodhead, doing business as T. H. Brodhead Company. The record should show that counsel stipulate that T. H. Brodhead—or T. H. Brodhead Company, rather, is a special partnership organized on or about October 1st, 1942, which was in existence at the time Chapter 225 of the Revised Laws of Hawaii, 1935, was repealed by Act 162 of the Sessions Laws of 1943. In other words, it was a special partnership governed by the law before the uniform act. The question had come up when the

case was tried before as to Mr. Brodhead who was the general partner appearing to represent the whole partnership, and that was covered by the law governing this partnership, that we agreed and the record shall contain that stipulation.

The Court: That's agreeable to counsel?

Mr. Cades: Yes, that's agreeable. [45]

The Court: That is to say, the law as it was in the Revised Laws of 1935 as amended?

Miss Lewis: Yes.

Mr. Cades: The uniform partnership act which repealed the section on special partnerships had a saving provision to the effect that those that were previously registered would be governed under the old law.

The Court: Yes.

Mr. Cades: Does that dispose of everything that we had agreed on?

Miss Lewis: Yes, I think it does.

Mr. Cades: Now, then, at this time I would like to offer in evidence, or possibly some stipulation could be agreed on with regard to the tax primer. By way of introduction I might state that it is our contention—that among our contentions is one that the method of administering the laws from 1935 until 1942, without any amendment in the law, is of importance, and that it's also of importance in construing the meaning of the act itself to see how the taxing authorities administered it, how they understood the law from the time that it was first enacted. In other words, it's our belief that if a law is enacted which may be doubtful in its mean-

ing, the interpretation put on it by the persons charged with the administration of the act is of importance in determining the meaning of the act; of course it shows what they understood and what the public should have understood and what property the Legislature meant by the act at the time, particularly since they allowed that practice to continue. In that connection we wish to put in evidence the tax primer as evidence as to how the administrative officers acted. The tax primer itself is [46] dated July, 1935, and it is put out over the imprint of "Territory of Hawaii," with the request that any additional information can be obtained from the Honorable William Borthwick, Tax Commissioner.

Miss Lewis: I object to the introduction in evidence of the tax primer on the ground that it is incompetent, irrelevant and immaterial, and I would like to make my argument on that point if counsel has concluded with his offer.

The Court: Well, I think first the offer should be clarified or at least the objector should clarify the objection, one or the other, as to whether there is any question of the promulgation of the document, whether or not it has any competent factors or relevant bearing upon the issue as to the ultimate question; but I don't want any error in the record to appear from a careless treatment of identification of the document itself.

Mr. Cades: If you'll pardon me—it's probably my error, but I meant to state that I believe that counsel will stipulate as to the fact that Mr. Westly

would testify that this was issued by the Tax Commissioner, that it was issued for the purposes stated in the primer itself, and that it was distributed to the public for the purposes stated in the primer; and I just assumed that we would arrive at some such stipulation later in accordance with our prior conversation once the question of its administration, assuming that it comes from proper sources, is established.

The Court: Well, I think that perhaps you better identify it by a number so that the record indicates what you are talking about; call it Plaintiff's No. 1.

Mr. Cades: Well, I don't know what exhibit—we already have some exhibits— [47]

Miss Lewis (Interrupting): We have a Defendant's Exhibit 1—

Mr. Cades: A, B, C, D, E, is it?

The Court: You mean those exhibits attached to the stipulation?

Mr. Cades: No; they're attached to the transcript; we have a record of those.

The Court: Well, suppose you number this "A-A?"

Mr. Cades: Yes, that would be—

Miss Lewis: Well, that is putting a number for identification only, is it not?

Mr. Cades: Yes.

The Court: Yes, identification No. AA refers to the so-called tax primer that counsel has been talking about. Now, do I understand, Miss Lewis, that to itself as a printed document you are or are not

ready to stipulate that the witness named by counsel would, if sworn and testifying, identify it as a document emanating from the Tax Office?

Miss Lewis: Yes, as a matter of foundation and subject to the objection as to the competency, relevancy and materiality, I'll stipulate that this pamphlet was prepared and caused to be printed by the Tax Commissioner and was distributed by the Tax Office. It, as it states, is not a compilation of any rules or regulations; as it states——

Mr. Cades (Interrupting): May I interrupt one moment; before you go into an argument can we finish with the stipulation as to what it is, as to what you agree that it is, and then we can argue about it. Of course there are a couple of other things that I'd like to enter into the stipulation as to what Mr. Westly would testify. [48]

The Court: Well, you might make that in the form of an offer of proof by Mr. Westly and see if Miss Lewis is willing to stipulate that if he were sworn and testified he would substantially support those facts.

Miss Lewis: I think I was not going into argument, Mr. Cades; I was going to read from the foreword to show that this pamphlet is. In other words, in my statement that this pamphlet was prepared and caused to be printed by the Tax Commissioner I had not covered the nature of the pamphlet; I wanted to cover that in the foreword of the pamphlet itself. I think the record might well contain that statement which is in the foreword of the pamphlet as part of——

Mr. Cades (Interrupting): Well, I referred to that; I stated in my offer that it was inserted by the Tax Office for the purposes stated in the manual, or in the primer.

The Court: That is, your offer is inclusive of the qualifications, conditions, and so forth that the primer itself expresses?

Mr. Cades: Yes, that's correct.

Miss Lewis: Very well.

The Court: And in lieu of examining Mr. Westly on that you are willing to stipulate, Miss Lewis, that if called he would identify the pamphlet as emanating in that respect from the department?

Miss Lewis: Yes.

Mr. Cades: I would further like to prove by Mr. Westly that it was distributed to the general public beginning in 1935 and until some time around January, 1942, and that insofar as question and answer number 59 are concerned, contained in the primer, that no different information other than contained in that question and answer was [49] ever given to the public until the publication of the notice, being Defendant's Exhibit 1, which was approximately January 1st, 1942.

Miss Lewis: Well, that is correct as a statement of fact subject to the objection as to competency, relevancy or materiality.

The Court: I would make clear in the record that any and all questions as to admissibility, competency or relevancy of the testimony will await the conclusion of the identification of the document.

Mr. Cades: Well, that concludes my offer by

way of identification; and at this time I would like to offer in evidence Plaintiff's Exhibit A-A for Identification.

Miss Lewis: And I'll renew my objection on the ground of incompetency, immateriality and irrelevancy. The Supreme Court has held—that appears on page 4 of the advance sheet—that the gross income tax law expressed and intended—I'll quote from the Court, beginning with the words “an intent” I am quoting from the Court: “an intent clearly and unequivocally expressed.” That intent, the Court made clear, was that this gross income tax should apply to sales or rather proceeds of sales to the United States and its departments and agencies if they were not actually beyond the taxing power of the Legislature. The Supreme Court having held that this tax law did express that intent without any ambiguity, it is not competent to receive any evidence as to administrative construction; that's everything relevant in any event only where there is an ambiguity in the law; citing *Ewa Plantation Company vs. Wilder*, 26 Hawaii, 299, at page 316; that case was affirmed in 289 Fed. 664. [50] In the second place, the record already shows that in fact tax was not collected on the proceeds of sales to the United States until January of 1942. This is offered as cumulative evidence of the same thing but has no value because there was no occasion to construe the law with respect to a specific legislative exemption not founded on constitutional immunity until the time of the *King and Boozer* case. In other words, counsel is offering this, as

I understand it, not merely to show that in fact the tax was not collected until January, 1942, on sales to the United States, but in an attempt to show that someone, administrative officials or legislative, put certain interpretation on the words of the law itself. Now, there was no occasion whatsoever to interpret the law as to whether it meant that there should be such exemption as a matter of legislative grant thereof even though it was within the taxing power of the Legislature, until it appeared clear that that taxing power existed. After the King and Boozer case as to that power was clarified the Tax Commissioner did commence collecting taxes. If he had continued his prior practice after that time there might be some shadow of argument that he did so on the theory that there was an express legislative exemption, and had the Legislature then met and remained silent there would be some shadow of argument that they approved that. On the contrary, however, when the issue as to the question of whether there was an express legislative exemption not founded on constitutional immunity arose, at that time the Tax Commissioner took the position that there was no such legislative grant; and not only that, but the next Legislature by its legislation showed that it knew of the Tax Commissioner's action [51] in taking that position and approved it; so that the subject matter offered has no materiality even if the law were ambiguous, which it is not. In the third place, any administrative action which occurred before January, 1942, is explained by the fact that the Panhandle Oil Company

case, which is referred to in the opinion of the Supreme Court, was then the law and had not yet been overruled, and it is of no value whatsoever, even if this exhibit would show it, that the Tax Office assumed that under the Panhandle Oil Company case it could not levy the tax. Such construction is of value only when it relates to a local law insofar as that was an opinion of administrative officials as to the Constitution of the United States or the Organic Act; that has no bearing. In the case of *Biddle vs. Commissioner*, 302 U. S. 373, 82 Law Ed. 431 at page 439, our Supreme Court has stated that administrative rulings made upon the intent of other legislative bodies, rather than the legislative body governing the official, are of no value whatsoever; those concerned an interpretation of British law. So, your Honor, there's nothing to be gained from any evidence as to what was thought about constitutional immunity during that period.

Finally, I take the position that this manual could never be of any value because it is merely a statement, of an informative character it is true, but issued with the express caution that it does not commit the Tax Office as to what it will do and that it is not a rule or regulation. I am quoting now from the foreword of this tax primer: "This preliminary manual of elementary information pertaining to the gross income tax Act is issued in advance of the rules and [52] regulations to be promulgated by the tax commission, with a view to meeting the urgent demands for explanations of the Act and of the application of the tax in transactions

of various kinds. This present manual is of a general nature and may be changed from time to time prior to the publication of the rules and regulations. It is not intended to take the place of rules and regulations, but rather to place in the hands of taxpayers, as quickly as possible, essential information in concise form for their guidance until rules and regulations can be prepared and published according to law."

Now, the authorities agree, in the case of Federal Internal Revenue Taxes, which is parallel, that a bulletin or office decision is not admissible as evidence of administrative construction because it is tinged with the warning that it has not the force and effect of law and that it would not commit the Department of Internal Revenue to any interpretation of the law, any more than the bulletin in this case. The Supreme Court has held, and also the Circuit Court of Appeals, that such interpretations, rulings and bulletins which are subject to that cautionary notice are not admissible in evidence to show administrative practice; *Helvering vs. New York Trust Company*, 292 U. S. 455; and to the same effect is *Cole vs. Commissioner of Internal Revenue*, 81 Fed. (2d) 485. Although that's an additional ground, I do think that the offer could be disposed of on the first ground alone, that the Court has ruled that the law has a certain meaning and that it is not ambiguous, and there is no occasion to admit evidence on the point.

Mr. Cades: It's my contention, if your Honor please, [53] that the tax primer is evidence of a

contemporaneous interpretation of the Act by the persons who are charged with its administration. As soon as the Act was passed by the 1935 Legislature it was to be carried into effect, I believe as of July 1st, 1935, by the Tax Commissioner; and this manual was promulgated with the idea of informing the public as to what was and was not taxable in certain instances. In connection with the item in question, question number 59, the question is very direct, under the heading "Sales Exempt From Taxation: Sales to Federal Government:" "59. Q. Are sales to the Federal Government or its agencies exempt from the tax? A. Yes. Such sales are specifically exempted in Section 3 of the Gross Income Tax Act." That's the information that was given to the public, and it was given to them for a period of 7 years during which time the Legislature met in 1937 and 1939, 1941, 1942 special session—1941 special session—there were four sessions of the Legislature during which the tax Act was administered in this manner. The Act contained its own delimiting provisions; it said that the exemption granted here shall continue until Congress shall permit the Territory to impose such a tax; and it is our contention that that administration had to continue until the limit of the taxing exemption had been reached. And it's our further contention there is nothing in the Supreme Court decisions, so far as I understand it—and I must confess that I don't completely understand it—there's nothing that I understand that would make this inadmissible in evidence.

Miss Lewis: In very brief reply, I won't again go into the proposition that the Supreme Court has said that the intent to impose a tax is clearly expressed; but taking up the question of the value of it even if there's an [54] ambiguity, it seems very clear that there is nothing in it to show the position taken that such sales were exempted even if the Constitution and Organic Act did not require that; in other words, the statement made here giving it the weight of a rule, which it was not—I don't stand on my objection on that ground—but taking it as it is, it's simply a statement that Section 3 had exempted such sales; well, on the assumption that they are associated, that there were constitutional immunities, it did; well, that assumption isn't worth anything if it was assumed that there were constitutional immunities, that isn't going to make one whit of difference because we get our law and constitutional immunity from the Supreme Court of the United States; it couldn't mean anything in that regard until it was understood that constitutional immunities did not exist; that about at the time of the King and Boozer case, at that time the Tax Office made it clear that it took the position that the law itself as a matter of legislative intent levied a tax and constitutional immunity did not exist; and in 1943, which was the first meeting of the Legislature after the issue had developed—no issue developed until that law as to constitutional immunity had been clarified—that 1943 Legislature in Act 81 of that session made it clear that they understood that the Tax Office was levying the Tax

on sales to the United States and accepted that as a correct basis for further legislation.

The Court: Well, as I understand the offer of proof as to the primer, it's that prior to the period on which this suit affected taxes the Tax Office had promulgated a different statement of their understanding of their duties.

Mr. Cades: That's correct. In other words, our [55] point is this, that from 1935 to January, 1942, the public was told that such sales were exempt, and that exemption grew out of the same Act. On January 1st, 1942, there were a series of advertisements published which stated that, commencing January 1st, income from sales to the United States previously exempt would be subject to tax. It's our contention that a tax does not spring out of a statute that has granted an exemption for approximately 7 years without some activating force that brings it into effect; that the force that could terminate the exemption is stated in the Act itself to be the permission of Congress to impose a tax; that no such Act of Congress was passed, and that the tax administrator could not on one day say it's exempt and the next day say it's not exempt without some legislation that gives the administrator that authority to impose the tax as of one day and not as of the previous day.

The Court: Well, from the Court's angle as to the admissibility, the Tax Office's regard of its area of duty under an Act which the Supreme Court now hands back to me as unambiguous and material and relevant, therefore the opinion promul-

gated and distributed by the Tax Office for the years prior to the years affected by this suit are clearly incompetent, irrelevant and immaterial to my mind and therefore the offer in evidence will be denied.

Mr. Cades: May I have an exception.

The Court: Exception allowed. The document itself should stay in the file as so identified. Now is there any more of this?

Mr. Cades: No, that concludes——

Miss Lewis (Interrupting): That concludes the evidence for the defendant also.

The Court: Oh, a question—— [56]

Miss Lewis (int.): I have prepared findings of fact and conclusions of law embodied in a decision, your Honor, on the basis of the Supreme Court's opinion, and I would move that this decision be entered and the judgment be rendered thereon for the defendant. I so move.

The Court: I have a question in that regard as to whether it's necessary from all angles to take the record and the transcript and exception that you make part of the record in this case, or whether it can be assumed that I'll gather the pertinent material from a discussion of the proposed findings.

Mr. Cades: Well, from my standpoint, in order to shorten the proceedings—which I think is all we're interested in—I don't see why a judgment cannot be entered in accordance with the decision of the Supreme Court without any conclusions of law; and as far as findings of fact are concerned it's a very short record; there's no character or reputation

evidence; there's nothing really that requires finding certain facts; most of these are copies of stipulated facts; there's very little else.

The Court: Have you seen the form of this, Mr. Cades?

Mr. Cades: I have, yes.

The Court: Well, is there any particular part of it that raises a particular issue of the court of record on this theory that the Supreme Court has crystalized in its opinion?

Mr. Cades: Well, the only thing is, your Honor, that there has been no finding to admit with regard to the evidence as to the prior period which of course my objection to the finding of any facts is that it's incompetent, because if the Court will not admit the tax primer obviously [57] it will not enter findings as to what the Tax Office did during the period 1935 to 1942.

The Court: Well, let's look at the beginning of page three, the first paragraph of findings of fact; is there any dispute as to that?

Mr. Cades: No, there isn't.

The Court: And paragraph two, any dispute as to that?

Mr. Cades: No.

The Court: Any as to paragraph three?

Mr. Cades: No.

The Court: And as to paragraph four?

Mr. Cades: No.

The Court: Paragraph five?

Mr. Cades: No.

The Court: Paragraph six?

Mr. Cades: I have not checked the figures, but subject to that check—that's taken right from the stipulation.

The Court: Subject to correction for omission or error on those figures?

Mr. Cades: That's right, it's correct.

The Court: There might be a typographical error.

Mr. Cades: Yes; we can compare that with the stipulation which is in the record.

The Court: Yes. Paragraph seven?

Mr. Cades: No objection.

The Court: Paragraph eight?

Mr. Cades: No objection.

The Court: Nine?

Mr. Cades: No objection.

The Court: Paragraph ten? [58]

Mr. Cades: No objection.

The Court: Paragraph eleven?

Mr. Cades: With regard to the language of it, with regard to it in general, the examples are what I object to in there; I have no objection to the general statement.

The Court: Well now, what part of it is it that you think is unnecessary?

Mr. Cades: Beginning with "for example," the rest of that sentence, beginning on the sixth line "for example."

Miss Lewis: As a statement of fact based on the evidence of Mr. Westly, that is correct though, isn't it, Mr. Cades?

Mr. Cades: No, it wasn't because there was some difference between the utility companies even; the Gas Company and the Electric Company were on different bases, and although the purchasers—what I mean by that is that the Electric Company, I believe it was, was divided into two parts; certain of their sales were exempt and yet the purchaser itself was subject to gross income tax, it may not have been with regard to particular sales; so that that in my opinion doesn't make it a correct statement.

The Court: Is there any necessity for that explanatory language in the findings?

Miss Lewis: Yes, I think it definitely is part of the record and should appear in a finding; and as to Mr. Gates' statement that is certainly a true summary of the evidence that it is covered here because what is mentioned is sales of stoves, refrigerators, heaters, and other goods to public utilities which resell but pay the public utilities tax in view of the general excise tax on the resale of such [59] goods; to the extent that they carry a line of goods which is not subject to public utilities tax the finding will not apply.

The Court: Well, what I have in mind, Miss Lewis, is the pertinent issue in this particular case, it's a tax on the sales to the Post Exchanges and Ships Service Stores included under that term, and this illustration material that you have here is really going out of the picture that we're concerned with, isn't it?

Miss Lewis: No, I think not, because it might be important for the record to show that the Post Ex-

changes were not the only such cases involved; that there were other similar cases and they were all treated the same. It might be thought otherwise that something had been done by design because the Post Exchanges alone would fall into the net; and I think it's important to show that there were other such situations in the course of normal practice and they were all treated the same.

The Court: Well, after you cover that so far as findings of fact need to cover it, the evidence itself would pick it up as to things detailed by the first 5½ lines: "In instances in which sales are made to purchasers other than post exchanges and ships' service stores, classified by the Tax Commissioner as not subject to tax under the General Excise Tax Law," and so on, even though he's assessed the tax, even though the goods were sold for resale.

Miss Lewis: I think it's important for the Court to find that there were other such instances besides sales to Post Exchanges.

The Court: The point I'm making is that if I'm going [60] to cite instances I've got to be careful that I cite them all or at least qualify the recitation so as to indicate clearly that I'm not citing them all.

Miss Lewis: Well, isn't that done by the words "for example?"

The Court: Not unless you've got some qualifying words.

Mr. Cades: Well, I might point out, for example, there's considerable doubt as to whether sales of food to schools classified for resale is an analogous instance, because the food in general in its character

in many instances, it isn't the same food that is resold necessarily; there may be an ambiguity by such findings that the Court finds that would be very similar to the resale of jewelry by ships' service stores, which I don't think the Court would like to do without some consideration.

The Court: Well, I don't frankly see the necessity of the Court attempting to illustrate unless the Court goes into the entire record and picks out of that record only those features that illustrate or clearly indicates by qualification that it's not attempting to be inclusive; and, secondly, that any raising of an example defeats the finding if the Appellate Court finds that the example is not well taken. I think that the matter that the 11th finding covers is sufficiently covered by putting a period after the word "purchaser" in the sixth line of the finding, and eliminate the balance of the paragraph.

Miss Lewis: Well, will the Court substitute for those words stricken out the following: "Sales to Post Exchanges were not the only instances of sales made to persons not subject to the General Excise Tax who intended to resell them?" [61]

The Court: Well, that's covered by the language even though the goods were sold for resale by the purchaser.

Miss Lewis: Well, there is a specific situation which I think should be covered by a finding of fact; the evidence does show definitely, this being findings of fact, as to what was done by the Tax Office; the record definitely shows that the Tax Office did as a

matter of administrative finding classify other sales besides sales to Post Exchanges as subject to tax at $1\frac{1}{2}\%$, on the ground that the purchaser was not subject to the General Excise Tax, and including other purchasers, who intended to resell.

Mr. Cades: I think that's all covered in that first sentence.

Miss Lewis: It's not if that does not include a finding that there were actually other instances besides the sales to Post Exchanges.

The Court: I would admit this possible clarification, that after the word "tax" on the fourth line where the third line comes down "he has assessed the tax," "in a non-discriminatory manner."

Mr. Cades: Well, I'm not sure that that is the evidence; I think it's a conclusion of law that could only arise out of a reading of the whole record.

The Court: Well, he has assessed the tax without apparent discrimination.

Mr. Cades: Well, I think as soon as you get into discrimination that's properly a question of law because discrimination is a word of law in tax matters.

The Court: Well, I'm covering the factual side; "without discrimination in fact." [62]

Mr. Cades: Well, I think that's very difficult to say without the record, and I don't think there is much evidence in the record.

The Court: Well, I think, to simplify the issue that I'm proceeding with here, the Court is willing to take the first $5\frac{1}{2}$ lines just as they are here and eliminate the balance of that sentence and take the

last short sentence "Such practice was followed throughout the period in question."

Miss Lewis: Well, if the Court please, to make a finding of fact that there were other such instances there should be added to that statement "Such practice followed throughout the period in question"—and this would be the addition after "goods"—"and was applied with respect to sales to a number of persons, not Post Exchanges merely"; something of that character should be included.

The Court: Well, I think what you want here is more appropriately covered, if at all, in the opening words of—"In instances in which sales were made to purchasers other than Post Exchanges."

Mr. Cades: I think that would cover it.

The Court: See where I got that?

Miss Lewis: Yes.

The Court: "Other than Post Exchanges"; applied by the Tax Commissioner; that carries what you're after, I think, right straight into the conclusion.

Miss Lewis: Yes.

The Court: And then just leave the last sentence as it is: "That practice was followed throughout the period." That leaves it open to the details of the evidence record itself, and it doesn't jeopardize my findings as being inclusive of the wrong things and exclusive of the right things. [63]

Miss Lewis: Yes, I think that does cover it; and I thank you for it.

The Court: Now as to "Conclusions of Law."

Mr. Cades: Might I at this time request additional findings of fact?

The Court: Have you got them worked out?

Mr. Cades: I haven't but I could—I think I could recite them fairly approximately.

The Court: Well, the question in my mind, Mr. Cades, whether or not it wouldn't be more of value for you to tersely reduce them to writing and let Miss Lewis have a copy of that proposed addition so that we can have a session and hearing; she may agree to what you have as being a correct summary of the record, and if there is disagreement then thresh them out; wouldn't that be more logical?

Mr. Cades: Yes, I think probably it would; I could do that by some time this afternoon, and then if you have some time tomorrow morning; I don't think we would need much time.

The Court: Well, the only caution I have to give is that I don't want to rewrite the transcript in the decision.

Mr. Cades: Yes, I understand.

The Court: Well, so that I can be sure that I'll have time for you and that Miss Lewis will have time to go over your preparation, if you get your preparation over to her by either late this afternoon or first thing tomorrow, then I can have a session on Friday morning; that fits in with my calendar better.

Mr. Cades: Friday at nine?

The Court: At nine o'clock, yes; that's the 10th.

That will give you a day to chew over the language together. [64]

Miss Lewis: All right.

The Court: And let me pass this original back to you; that page 7 will have to be modified anyway and it will be left open for any additional findings of fact that you may either agree to or the Court inserts.

Mr. Cades: Can we go on with conclusions of law now?

The Court: Yes; maybe we can clarify those.

Miss Lewis: Of course I may want to add something to that at the same time.

The Court: Paragraph "A" of Conclusions of Law.

Mr. Cades: No objection to number one—or "A".

The Court: And "B"; that's the Supreme Court's determination, isn't it?

Mr. Cades: That's right, yes, that's correct.

The Court: And "C"; that's also the Supreme Court's conclusion in its opinion?

Mr. Cades: Well, I'm not sure of that wording. I wonder, Miss Lewis, if you can point to that statement of the Court; I don't have the printed copy.

Miss Lewis: Well, it's there because they ordered judgment reversed, did they not; the Court held that with respect to the meaning of Section 3 of the Act it's not material.

The Court: Well, it says on the bottom of page 314 "whether or not the effect of the decision in the Panhandle case was to extend constitutional immunity under use of the language contained in Section 3 of the Act.....of the legislature." I think

the inference in that language is that the Supreme Court has thereby concluded the language in Section 3 is as granting an immunity, it's construed.

Mr. Cades: Well, I think that their statement should [65] be amended "that Section 3 of during the period in question under the tax," in this case, because it certainly did exempt the sales to him in previous periods.

Miss Lewis: Well, if the Court please, obviously there's no ruling on anything that's not before the Court, the kind of language he injects in an issue that isn't before the Court at all.

The Court: Well, I think that that would be clarified by putting a comma at the end of that finding and the words "as applied to any of the issues of this case."

Miss Lewis: Well, wouldn't it be better to refer to the finding number six, "that Section 3 of sales."

The Court: Covered by paragraph six of the findings of fact?

Miss Lewis: Yes; made by him.

The Court: Any language of that character will tie it expressly down to the case.

Miss Lewis: I'll modify finding six.

Mr. Cades: Yes; that will make it an accurate statement, "made by him."

Miss Lewis: Of sales covered by finding number six made by him to the United States Government and Post Exchanges.

The Court: That ties it down.

Mr. Cades: Yes, to this particular sale.

The Court: Now "D"?

Mr. Cades: No objection.

The Court: "E"?

Mr. Cades: No objection.

The Court: "F"?

Mr. Cades: No objection.

The Court: "G"? [66]

Mr. Cades: When I say "No objection" I mean as to the form of the language; I don't see the file.

The Court: I understand your objection to the result is inclusive and continues throughout; and the record should show counsel's reply to the Court in this matter is as to the form of the language and not as to the ultimate result on which he is taking an adverse position.

Mr. Cades: That is correct.

The Court: "G" is also within the direction—

Mr. Cades (int.): Well, "G-1", I don't think that that is quite true with regard to public utilities, and I think the language here would have to be tied up closer with the language of the Court that covers it.

Miss Lewis: Well, it is covered by the words "and others not subject to a second tax."

Mr. Cades: Where is that language?

The Court: That's the fifth line.

Mr. Cades: Yes, but I mean in the Court's decision because we know as a matter of practice that it isn't true, that there are a number of second and third instances of taxes of $1\frac{1}{2}\%$; of course if it were

made by the Court I couldn't object, but as a matter of fact I don't think it's correct.

Miss Lewis: I don't get the point there, Mr. Cades.

Mr. Cades: Well, it isn't true that in all instances where others are not subject to a second tax, $11\frac{1}{2}\%$ is the tax that's paid; in other words, there are sales at one-quarter of one per cent where the merchandise is sold outside the Territory, and still the tax is one-quarter of one per cent, only, not $11\frac{1}{2}\%$; there are a number of instances where there is no second tax.

Miss Lewis: Why don't we say "—within the Territory?"

Mr. Cades: Well, there may be other exceptions there.

Miss Lewis: Well, I don't know what they are.

The Court: Well, after the word "others"—"and others in similar position subject to a second tax?"

Mr. Cades: Well, I don't think that is the test; it's others who are not licensed dealers, or something of the sort; it was better stated in the finding of fact; in other words, it's on sales to purchasers who are not subject to tax under the General Excise Tax, it isn't that they are not subject to a second tax, it's others not subject to the General Excise Tax Act.

Miss Lewis: All right; let's say "and others not subject to general excise tax."

The Court: Instead of the word "second."

Mr. Cades: Then we could strike out all about the rate.

Miss Lewis: What was that?

Mr. Cades: Oh, I see; no.

The Court: Any modification of sub-paragraph 2 under that "G"?

Mr. Cades: No.

Miss Lewis: Excuse me; we had one change we inserted under excise tax—; did we also insert "sales within the Territory?"

The Court: No; we left the language of the paragraph alone except by striking the word "second"; this is paragraph 1; striking the word "second" and putting in "general excise." Now paragraph "H".

Mr. Cades: That's all right.

The Court: Paragraph "I" [68]

Mr. Cades: That I don't think is quite right. I think that what the Court said was that they were not merchants; that's on the bottom.

The Court: You eliminate the word "retail?"

Mr. Cades: Yes.

Miss Lewis: Well, I think it's an immaterial thing.

The Court: Well, you can fix that up.

Mr. Cades: Well, it makes the error more apparent when you leave out "retail."

The Court: "J"? That's the majority opinion.

Mr. Cades: "J" is all right.

The Court: "K"; I think that's what the majority opinion plus the minority opinion both hold, binding upon this Court.

Mr. Cades: Well, I don't think the minority holds that.

The Court: Oh, no; the majority opinion does hold, and hereby its finding says it's discriminatory if it's $1\frac{1}{2}$, it's not discriminatory at $\frac{1}{4}$.

Mr. Cades: Well, that's what this has reference to, clarifying between $\frac{1}{4}$ and $1\frac{1}{2}$.

The Court: Yes, this is the ruling of the majority opinion.

Mr. Cades: Well, I was wondering if that was the language, that it was "natural and reasonable"; they held that it was not discriminatory.

The Court: Read that language toward the end there.

Mr. Cades: Yes, they do say that.

The Court: Any other modification of "K"?

Mr. Cades: No, that's all right. [69]

The Court: "L"?

Mr. Cades: No, no objection.

The Court: "M"?

Mr. Cades: Well, I'm not sure of "M." Is that anywhere in the opinion?

Miss Lewis: I think really the Court didn't go into that argument you made.

Mr. Cades: No, I don't think so either.

Miss Lewis: Apparently they didn't consider it necessary to do so.

Mr. Cades: Well, going back to "L"; did they go into "L"?

Miss Lewis: Well, that was in the decision disposing of the rehearing; it's very clear in there.

Mr. Cades: I see. Well, "L" I have no objection to. "M" I think goes further than four does.

Miss Lewis: Well, it's true they didn't go into that matter; if it isn't material, it isn't necessary to be in there.

The Court: I don't think it's necessary for me

to go there; let the Supreme Court clarify their own language.

Mr. Cades: And I can't object to "N" or to "O" either.

The Court: All right. Now, if you have in setting down suggested additional findings of fact that you think the Court should pass upon, and also while you're doing it it occurs to you that the Court should rule in the decision on any matters of law that I haven't covered by this language, draft those up and submit them to Miss Lewis, and what you can agree on, all right; if you can agree on them we'll have a conclusion on Friday morning. [70]

Miss Lewis: Well, I think the retyping might well be held, then, because it would be hard to finish all the pages.

The Court: Yes; you can't go beyond "Findings of Fact" in retyping until you get all the additional material.

Miss Lewis: Yes.

The Court: All right.

May 15, 1946, 2:10 P.M.

The Court: Preserving all exceptions and objections that the plaintiff has heretofore entered of record, the form of the decision I understand you have no new objections to it?

Mr. Cades: That's correct, not to the form.

The Court: So that the decision, with that one change of wording in the "nth" paragraph, you have no other matter to bring to my attention for change of wording?

Mr. Cades: That's correct. I'd like to note an exception to the decision on the ground that it's contrary to the law, the evidence and the weight of the evidence.

The Court: Exception may be noted.

Mr. Cades: At the same time I'd like to except to the entry of judgment on the grounds that the judgment is contrary to the law, the evidence and the weight of the evidence.

The Court: And inclusive of all objections made, reiterated during the progress of the trial and on the record.

Mr. Cades: Correct.

I Hereby Certify the foregoing to be a full and accurate transcript of my shorthand notes taken in the above entitled cause.

/s/ OLAF OSWALD,
Court Reporter.

[Endorsed]: Filed Aug. 10, 1946. [71]

In the Circuit Court of the First Judicial Circuit,
Territory of Hawaii

L. No. 16956

THOMAS H. BRODHEAD,

Plaintiff,

vs.

WILLIAM BORTHWICK, Tax Commissioner and
Tax Collector,

Defendant.

TRANSCRIPT OF TESTIMONY AND
PROCEEDINGS

The above-entitled matter came duly on for hearing before the Honorable John Albert Matthewman, a Judge of the above-entitled court, jury waived, on June 16, 1943, at 9 o'clock a.m.,

J. Russell Cades, Esq., and Milton Cades, Esq., of the firm of Messrs. Smith, Wild, Beebe & Cades, appearing for the plaintiff herein, and

J. Garner Anthony, Esq., Attorney General, and Miss Rhoda Lewis, Deputy Attorney General, appearing for the defendant herein,

Whereupon the following proceedings were had and testimony taken:

Mr. Milton Cades: Ready for the plaintiff, your Honor.

Miss Lewis: Ready for the defendant.

The Court: Proceed.

Mr. Milton Cades: This is an action to recover gross income taxes paid under protest. The parties have entered into a stipulation covering many of the

facts involved, and have reserved the right, first, to question the materiality of the [74] facts set forth, even though we have stipulated to the facts; we reserve the right to question the materiality of the facts, and we also reserve the right to produce evidence upon the trial. In connection with the stipulation, too, we have reserved the right to amend it in conformity with the original drafts, which were checked, and this final draft has not been, and if any errors are found the right is reserved to make those changes.

It is further desired, in connection with this matter,—there are a lot of figures set forth, and it is very difficult for almost anybody to make anything out of them except the parties who have lived with them for awhile, and we believe that if the issues are decided that the amounts involved can be agreed upon by the parties, so that we would request that the judgment,—or, rather, the opinion, need not necessarily include the amount of refund or the amount to be included in the judgment, but that that can be computed by the parties and included in the judgment.

The Court: Look at it this way: There is the complaint alleging facts. It is incumbent upon the plaintiff, naturally, to establish the fact. Now oftentimes that is done by stipulation; the other side agrees with the plaintiff that certain of the facts are true. That simplifies things greatly. We get rid of this and we get rid of that, and then we have left just the matters in issue. May we do that in this case?

Mr. Milton Cades: Yes, your Honor.

The Court: All of these,—there are quite a number of allegations, which undoubtedly you will consider it necessary to prove, to make up your case, according to the complaint. Now instead of putting the witnesses on the stand to go over [75] all of this, I am supposing from what you have just said that the other side has agreed with you that a large part of this is true, is that correct?

Mr. Milton Cades: That is correct, your Honor.

The Court: Then would it not induce toward a clarification to have you state now, paragraph by paragraph, what facts are admitted, and then the rest of it, only, you have to prove?

Mr. Milton Cades: Yes, that can be done, your Honor. May I at this time offer the stipulation, which has been agreed upon by the parties.

The Court: It may be received and filed.

Mr. Milton Cades: In connection with this stipulation there are some further facts which are agreed upon, which I would like to have made a part of the stipulation, and subject to the same terms.

The Court: Do you wish to do it this way? What you have there you have put in writing?

Mr. Milton Cades: Yes.

The Court: You might state now, for the record, these other facts as to which both sides agree, and they will be taken down.

Mr. Milton Cades: Yes, and if the court desires we can file a supplemental stipulation covering these facts.

The Court: If you care to, you can now state for the record what you stipulate.

Mr. Milton Cades: First, that purchases are made by post exchanges both on the mainland and locally according to the best judgment of the exchange officer.

The Court: May I interrupt you again, Mr. Cades. I do not know anything about this case. Would you preface whatever you have by giving me some idea as to the case. It is for the [76] refund of these income taxes paid under protest?

Mr. Milton Cades: That's right.

The Court: Are there several matters of issue? Are they issues of fact or are they issues of law? I would like, as soon as convenient to you, to learn what are the issues. Are they issues of fact or issues of law, or both?

Mr. Milton Cades: Yes, I will be glad to make a statement on that.

The plaintiff is Thomas H. Brodhead, who is a resident of Honolulu, and the defendant is William Borthwick, Tax Commissioner and Tax Collector. The plaintiff made monthly gross income tax payments for each of the months of January to September, 1942, and in his reports he showed varying amounts as his retail and wholesale sales, and made a note on the back of the returns to the effect that the tax paid on government sales is paid under protest, pending any court decision on the matter. The tax commissioner made an assessment of taxes, and made demand for the payment of additional taxes, and the taxpayer paid \$2,631.10 under protest.

As the issues involved are all matters of law, we have agreed to the kind of sales that were made. We have stipulated as to the amount of sales of each class, and as to which sales are properly taxable and which sales are in question. The sales in question are, first, sales to the United States which are assessed at $1\frac{1}{2}$ per cent., and those sales, we contend, —the plaintiff contends, are not properly taxable, because they are assessed in violation of the tax law and the Organic Act, and the Constitution of the United States. That is one of the issues involved.

Another issue is a purely technical issue of whether the assessment as a whole is not illegal, because it is made [77] upon the monthly returns or estimated of the taxpayer, and it is the plaintiff's contention that the assessment can only be based on the annual report and not on the monthly report.

And the third contention has to do with sales to post exchanges which are sales for resale. It is the plaintiff's contention that those sales cannot be taxed at more than $\frac{1}{4}$ of 1 per cent., even if they can be taxed at all. The argument there is, first, that the post exchanges are instrumentalities of the United States, and as such they fall within a class of all other sales to the United States. If the court finds that sales to the United States can be taxed, then we claim that they can only be taxed at $\frac{1}{4}$ of 1 per cent., and not at $1\frac{1}{2}$ per cent., and that is based on our contention that a post exchange is greatly like any retail store, except that they are not required to have a gross income tax license, because

they are not required to be licensed, and we contend that they cannot be charged a higher rate of tax. That is, it is a discrimination against a United States agency and instrumentality, based upon an unreasonable classification.

All of the facts, or the vast majority of the facts in this case are agreed to, and the issues are chiefly issues of law.

The Court: But there are some issues of fact, I take it, are there?

Mr. Milton Cades: Well, I don't know of any. Frankly, I don't know of any issues of fact.

The Court: Well, then, how does this strike you? It is incumbent upon you to get before the court the facts contained in your complaint. You have done that entirely, now, by stipulation? [78]

Mr. Milton Cades: No, we still will require some evidence, your Honor.

Mr. Anthony: You haven't completed your stipulation, either, which you were about to read.

Mr. Milton Cades: Yes, that is true.

No, some of the facts will be supplied by this additional stipulation, and there will be some evidence.

The Court: Yes, I think I interrupted you, Mr. Cades.

Mr. Milton Cades: To get back to the stipulation, first; purchases are made by post exchanges both on the mainland and locally according to the best judgment of the exchange officer, the delivered cost to the exchange being one of the most important factors considered.

2. Goods purchased from the plaintiff were purchased for sale by the exchange to authorized per-

sons and organizations in accordance with paragraph 13 of the Regulations, which is Exhibit E, and such authorized persons and organizations bought such goods from the exchange for their own use or consumption and not for further sale.

3. The post exchanges operate stores, as authorized by paragraph 10 of the Regulations, Exhibit E, and with the exception of goods sold to authorized organizations the goods bought from the plaintiff were sold in such stores in small quantities to each purchaser.

Mr. Anthony: If the court please, at this time I would like to have the record perfectly clear that we join in this stipulation subject to our objection that we insist that this stipulation is immaterial, and we will argue that to the court at the appropriate time. This is on the same basis as our objection to the written stipulation, which contains a recital [79] of certain facts which we will also argue, although stipulated to, are immaterial to the issues of this cause. I wanted to make that clear to the court at the outset.

MORTIMER J. GLUECK

was duly called and sworn as a witness for the plaintiff herein, and testified as follows:

Direct Examination

By Mr. Milton Cades:

Q. What is your name, please?

(Testimony of Mortimer J. Glueck.)

A. Mortimer J. Glueck.

Q. And what is your occupation?

A. I am a food broker, and also I have acted as an accountant for several firms.

Q. During the period January 1st, 1942, to September 30, 1942, were you the accountant of Thomas H. Brodhead? A. I was.

Q. And in that connection were you familiar with the business of Thomas H. Brodhead?

A. Yes.

Q. Were you familiar with the kind of business he did? A. Yes.

Q. And the organization of his business?

A. Yes.

Q. What was his business?

A. His business was principally supplying so-called ships' service or post exchange needs to both the Army and the Navy. That forms the greatest part of his business. That includes such items as candy, toilet articles and razors, fruit juices, and anything of that nature, belts, emblems; anything like that, that post exchanges or the ship's service stores might require [80] for resale to their men.

Q. Did he have any other customers?

A. He did, yes.

Q. What was the nature of the sales; were they large quantities or small quantities?

A. His other business, the rest of his business, was principally wholesale business.

Q. Principally wholesale business? A. Yes.

(Testimony of Mortimer J. Glueck.)

Q. And was he generally known in the trade as a wholesaler?

A. Yes, very definitely. He maintains a warehouse. He has an office force, and he has trucks and salesmen, so he forms a wholesaler in the general meaning of the term in the trade.

Q. And he sells to retailers and jobbers?

A. He sells to retailers and jobbers, yes.

Mr. Anthony: No questions on cross-examination.

(Witness excused.)

Miss Lewis: I would like to make a statement of the issues from our standpoint, your Honor.

The Court: Proceed.

Miss Lewis: The issues have been stated by the plaintiff, and I would like to make an additional statement, of additional issues, from the standpoint of the defendant. It is true that there is involved in the case the question of the taxation of the plaintiff on his gross income from sales to the United States and instrumentalities of the United States, but the defendant contends that arises only with respect to sales the gross income from which was included in the returns from July to September of 1942. The figures which are contained in this stipulation divide these into two periods. During the [81] period from January to June, 1942, the plaintiff was paying his taxes at the time when he was filing his returns, and although he made a notation on the back of each return that he was protesting pending court determination of government sales

taxability, actually he did not follow up that informal and brief protest by suing to recover the money so paid, within the required 30-day period. The statute, Section 571, R. 1935, under which the plaintiff is suing the tax commissioner, who represents the Territory, as we contend, requires that it be filed within a 30-day period. The reason for that is that the money is kept in a special fund to await the judgment of the court, if the suit is filed within the thirty-day period, and if it is not impounded there is no amount to meet the judgment, if the court so found, and we contend that the tax commissioner, representing the Territory, cannot be sued at this time. That perhaps could be better brought out in our argument, but I wanted to divide this period into two periods, because the plaintiff did not mention that fact.

With respect to the sales to the post exchanges, we share in plaintiff's desire that his objection to the rate of tax should be determined, assuming that the sale is taxable, as we contend that it was, but we feel it necessary to point out to the court that there is a subsidiary point, and that is whether the plaintiff is in any position to complain of that rate. He himself in his return did classify the income from those sales to the post exchanges as retailing, which means it is taxable at $11\frac{1}{2}$ per cent., if taxable, and he did claim the exemption, but he did show this income in the "retailing" column, and now he comes into court and says the money was illegally extracted from him, the only ground being [82] that it was not retailing but wholesaling, and

we feel that if the court should consider that the plaintiff's objection to the rate of tax has some merit, the court should further consider whether he is in a position to advance that point. So that is an additional point that the plaintiff did not mention.

There is a question, too, in the matter of cost, as prayed for in the complaint; the costs and interest, which is not in conformity with a suit against the Territory, which we are prepared to show is the proper way to consider this case. That is a very small issue, but one that was not mentioned by the plaintiff.

The Court: Are we proceeding under the assumption that the plaintiff's case is in?

Mr. Milton Cades: Before I rested I did want to make these reservations, that, as a part of my case, I did want to question Mr. Westly, but I am informed that the defendant is going to call him, and he has consented to my questioning Mr. Westly as if he were testifying as a part of the opening. That is, I will not be limited in the course of my cross-examination to the matters which he has been questioned on.

With that statement, we rest.

The Court: Let's follow this as regularly as you can. Do you have another witness now?

Mr. Milton Cades: I was going to call Mr. Westly as a part of my case.

The Court: Do you, or don't you? Let's take it regularly.

Mr. Milton Cades: Yes, I will call him.

TORKEL WESTLY

was duly called and sworn as a witness for the plaintiff, and testified as follows: [83]

Direct Examination

By Mr. Cades:

Q. State your name, please.

A. Torkel Westly.

Q. And you are the deputy tax commissioner in charge of gross income taxes? A. Yes.

Q. And what was your position before that?

A. Deputy tax commissioner in charge of field examination.

Q. And how long did you hold that position?

A. From August, 1937, to June, 1943.

Q. And how long have you been in the tax office, the Territorial tax office?

A. Since July 1st, 1935.

Q. In the course of your employment were you familiar with the administrative practice in connection with the assessment of gross income taxes and collection thereof? A. I believe I was.

Q. And with regard to sales to the United States, what was the practice of the Territory prior to January 1st, 1942?

A. Prior to January 1st, 1942, we considered sales to the Federal government as exempt.

Q. (By the Court): As what?

A. As exempt from the gross income tax.

Q. No gross income tax was assessed during that period prior to January 1, 1942, on account of sales to the United States, is that correct?

(Testimony of Torkel Westly.)

A. As we understood it at the time.

Q. Well, in the practice, you understood that such sales were exempt and you did not assess or assume to collect any taxes on account of such sales? [84]

Mr. Anthony: Just a minute. That is asking this witness a question with regard to what he understood. It is all right for him to tell what he did, but what his understanding of the law is, even the Supreme Court of the United States had to change its mind; that is why we are here; that is the question, your Honor.

The Court: Even on the view that it was permissible to go into what was done, is that really of some importance here? Is that important, what they had done with regard to cases of that sort? If so, why? No objection was made, but the thought comes into my mind on that question: Why is that helpful, what they had done?

Mr. Milton Cades: Because, if your Honor please, it appears that after January 1, 1942, there was a change made in the administrative practice, and the reason for it, I believe, is material in determining this case. In other words, beginning January 1st, 1942, the Territory attempted to collect and to assess taxes which had previously not been taxable, and in the absence of any change in the statute, we believe that that was an improper change in administrative practice.

The Court: This matter of administrative practice brings to mind the case in the Hawaiian courts

(Testimony of Torkel Westly.)

in the appeal of James A. Thompson. Maybe you gentlemen will recall it; a case that occurred while I was in the position Mr. Anthony now holds. In short, the Supreme Court held, with respect to the printing of Hawaiian Reports, which had heretofore been in the name of the clerk of the Supreme Court, and that although the Supreme Court itself had sanctioned that practice for 14 years, it made no difference whatever; that the contracts were void unless in the name of the Territory of Hawaii; that administrative practice counted for nothing, [85] when the law was otherwise. That is, these reports had been for 14 years been printed in the name of the publishing company and in Henry Smith's or James A. Thompson's, clerk of the Supreme Court—and the matter finally came up for a test, and the Supreme Court ruled on the test that it made no difference in the slightest what the practice had been, the law was just the same. Is that relevant to this matter?

Mr. Milton Cades: Well, in my opinion, yes.

The Court: Are you familiar with that case?

Mr. Milton Cades: Well, I have in mind a United States Supreme Court case where exactly that was in effect; it had to do with taxation under a Massachusetts statute of the proceeds of municipal bonds, and the Supreme Court of Massachusetts had held that the proceeds of those municipal bonds were not taxable, and upon a change being made the Supreme Court of the United States said, well, it was quite obvious that that change was directed

(Testimony of Torkel Westly.)

directly against the proceeds of those bonds, and indicates a discrimination directly against them.

The Court: Well, proceed.

Q. Mr. Westly, prior to 1942 did you assess for gross income tax and attempt to collect on account of the proceeds of sales to the United States?

A. Well, as I said before there is an exception. The sales to post exchanges, we did collect a tax from sales to post exchanges, which have since been held to be instrumentalities of the Federal government.

Q. Do I understand that before 1942 the only sales to the United States that were assessed for tax were sales to post exchanges?

A. Sales to post exchanges and ships' service stores. [86]

Q. Yes.

A. (Continuing): Where it is taxable, we considered them taxable, and we received a tax on sales to those organization prior to January 1st, 1942.

Q. And at what rate were they assessed?

A. One-quarter of one per cent.

Q. At one-quarter of one per cent?

A. Yes.

Q. But sales to the United States direct; that is, to the Army or Navy, or any other agency or instrumentality, except post exchanges and ships' service stores, were not assessed at all prior to January 1st, 1942?

A. That is correct. Of course there is an excep-

(Testimony of Torkel Westly.)

tion to that, too. We did tax contracts with the Federal government.

Q. That is, the proceeds of contracts?

A. With the United States.

Q. When you say "contracts" do you mean sales and purchase contracts, or just construction contracts?

A. I am referring to construction contracts only.

Q. It was only the proceeds of construction contracts that were taxed prior to January 1, 1942?

A. Yes, that's right.

Q. All other contracts of sales or purchases, or of other sales, were not assessed, except sales to post exchanges, which were assessed at one-quarter of one per cent?

A. That is correct.

Q. And the proceeds of construction contracts were taxed at what rate?

A. At one and one-half per cent, or one and one-quarter per cent, whichever rate was applicable.

Q. At one and one-quarter per cent, and then at one an one-half, when that rate became applicable?

A. Yes.

Q. On January 1st, 1942, what was the basis of the change?

A. You mean, why did we change it?

Q. Yes, why did you change it?

A. We changed it after receiving an opinion from the Attorney General to the effect that such sales could be taxed.

Q. And is that the reason also for increasing

(Testimony of Torkel Westly.)

the rate on sales to post exchanges and ships' service stores? A. Yes, directly, it was.

Q. That, too, was done because of an opinion of the attorney general?

A. Well, it refers to the same opinion. The opinion did not specifically mention post exchanges; it said "sales to the Federal government or its instrumentalities."

Q. During the period prior to January, 1942, the retail rate was $1\frac{1}{4}$ or $1\frac{1}{2}$ per cent?

A. It was $1\frac{1}{2}$ in 1941.

Q. In 1941. And when did that rate change from $1\frac{1}{4}$?

A. It changed, as I remember it, July 1st, 1939.

Q. When you talk of the $1\frac{1}{2}$ per cent tax, that means since July 1st, 1939?

A. That is correct.

Q. And the applicable rate for the prior period was $1\frac{1}{4}$?

A. Yes, and for six months it was one per cent, back in 1937; the rate changes occasionally.

Q. And that is ordinarily called the retail rate?

A. That is the retail tax rate.

Q. Now during the period referred to, all retailers—that is, all persons who sold, not for resale, were taxed at the rate of $1\frac{1}{2}$ per cent prior to January 1, 1942?

A. Well, there were others that were taxed at the same rate, even though the goods were resold.

Q. Yes.

(Testimony of Torkel Westly.)

A. The question was not whether it was for resale or not.

Q. That was not the question?

A. Not always.

Q. What was the question?

A. Well, for example a sale to an exempted institution for resale would be taxed at the retail rate. What I want to say is that "for resale" is not controlling, and has no direct bearing in determining whether the sale is taxable at the retail or wholesale rate.

Q. Well, all persons who sell for resale, and then resold, on their sales were taxed at $1\frac{1}{2}$ per cent, is that right?

A. You mean all persons who purchased for resale were taxed at $1\frac{1}{2}$ per cent?

Q. Yes.

A. They were, if they were subject to the tax.

Q. That is prior to January 1, 1942, and the same is true after?

A. The same is true after; if they are subject to the tax, they are taxed at $1\frac{1}{2}$.

Q. Well, to go back to that prior period; prior to January 1, 1942, all sales made to persons who resold were subject to a tax of $\frac{1}{4}$ of 1 per cent?

A. Not necessarily; there are exceptions to that rule.

Q. What were the exceptions?

A. The exception is as I said, a sale to an exempt institution.

Q. They did not resell?

(Testimony of Torkel Westly.)

A. Take a sale to a hospital; they may resell, or take a [89] sale to a school cafeteria, they resold, or any sale to a public cafeteria where they resell, but in such a case the sale is not to a licensed dealer, and not tax is paid on the resale.

Q. How about retailers, what were they taxed at; sales to retailers?

A. The sales to retailers, those who paid the tax on the resale, were taxed at one-quarter of one per cent, to the wholesalers.

Q. And were there any retailers who were not licensed, and the sales to whom were not taxed at the wholesale rate? A. I don't get that.

Q. Were there any retailers who were unlicensed prior to January 1, 1942?

Mr. Anthony: Do you mean retailers in the statutory sense or retailers generally?

Mr. Milton Cades: As he has been using the term.

A. There might have been some retailers that did not take out a license; if we knew about it we would see that they had a license.

Q. Yes, but do you remember in any instance taxing a person who sold to a retailer at the retail rate because the retailer was not licensed?

A. Not merely because the retailer was not licensed. If he was required to take out a license we would say that he was licensed, and we would allow the wholesaler the wholesale rate for such sales.

Q. So that it did not depend on whether the re-

(Testimony of Torkel Westly.)

tailer actually was licensed or not; it was dependent on whether he was required to take a license or not?

A. Yes, generally speaking, I think so. The tax commissioner [90] would give the taxpayer the benefit. If he sold to a person who should be a licensed retailer he would be allowed a quarter of one per cent. We would not penalize them just because the man did not take out a license and pay the tax as a retailer.

Q. Then do I take it that the reason that prior to January 1st, 1942, sales were taxed at $\frac{1}{4}$ of 1 per cent to post exchanges was because you believed they were required to take out a license; that is, post exchanges and ships' service stores were required to take out a license?

A. The ruling, and an agreement was made back in 1935 when the attorney general issued a ruling to the effect that post exchanges were not instrumentalities of the Federal government, and the taxpayers agreed to pay $\frac{1}{4}$ of 1 per cent on those sales, and the tax commissioner agreed to accept such tax.

Q. On January 1, 1942, was the rate increased because a determination had been made that post exchanges were not required to take out licenses?

A. No, the rate was increased because it was considered to be a sale to an instrumentality of the Federal government.

Q. Assume that the sale had not been made to an instrumentality of the United States, the tax would have been one-quarter of one per cent?

A. Well, it depends on to whom it was sold. As

(Testimony of Torkel Westly.)

I said before, if the sale was to a public utility it would not be a $\frac{1}{4}$ of one per cent; if it was to a school cafeteria it would not be $\frac{1}{4}$ of one per cent, but if the sale was to a licensed retailer who paid the tax, we would allow the one-quarter of one per cent to the wholesaler.

Q. Well, when you say "when it is made to a licensed retailer" you mean if it was made to a retailer who was required to take a license? It does not mean that he actually has a license; [91] it means that he is required to have it? Isn't that what you intend from your testimony?

A. Well, as I stated before, there are exceptions to the general rule, but if the buyer is required to have a license and should be licensed we will see that he is licensed, and if he is licensed and paying a tax we will allow one-quarter of one per cent to the wholesaler.

Q. But won't you also allow it if he is required to take a license and has not done it as yet?

A. Yes, I believe we would.

Q. So that is the only reason—— (interrupted.)

A. There are, of course, exceptions to the rule. If it is the fault of the seller that we did not license the buyer, then we may be more technical about it, and hold that the sale was not to a licensed retailer and as such we could not allow the $\frac{1}{2}$ of 1 per cent.

Q. But if it is not the fault of the seller, and if the buyer is required to have a license, whether or not he does have it, the seller would be taxed at the rate of $\frac{1}{2}$ of 1 per cent?

A. Yes.

(Testimony of Torkel Westly.)

Q. The increase therefore was made on January 1st, 1942, because as of that date it was determined that the post exchanges were not required to have a license?

A. As instrumentalities of the Federal government they would not be required to have a license.

Q. Yes, they were not required to have a license, and therefore the rate was increased from $\frac{1}{4}$ to $1\frac{1}{2}\%$ per cent?

A. Not merely because of the license issue; because it was a sale to the Federal government; an instrumentality of the Federal government.

Q. In other words, are all sales to an instrumentality of the [92] United States taxable at $1\frac{1}{2}$ per cent?

A. At the retail rate, beginning January 1st, 1942.

Q. And that is regardless of the purposes for which an agency or instrumentality of the United States purchases his goods? A. Yes.

Q. And that is regardless of the nature of the organization; of the nature or composition of the particular agency or instrumentality?

A. Yes, that is correct.

Q. And it does not matter what the instrumentality or agency does with the good after it purchases them?

A. No, it would not make any difference.

Q. And it does not matter whether they resell for consumption or use of the purchaser?

A. Absolutely immaterial.

(Testimony of Torkel Westly.)

Q. And it does not matter whether the agency or instrumentality uses it themselves?

A. That is absolutely immaterial.

Q. Now what you have testified to is what has been done by your office as a matter of administration of the tax?

A. That is right.

Cross-Examination

By Mr. Anthony:

Q. Mr. Westly, I notice that the title of this case is Thomas H. Brodhead versus William Borthwick?

A. Yes.

Q. Brodhead is the taxpayer?

A. He is the taxpayer.

Q. He is an individual doing business here in the Territory?

A. He is. [93]

Q. And he sells goods to various people including the post exchange?

A. He does.

Q. And the administration practice that you have described is that such a transaction under the gross income tax law that is taxable?

A. It is.

Q. And on what rate?

A. It depends on to whom the sale was made to; whether it was made prior to January 1st or after January 1st, 1942.

Q. Let's take one step at a time. In January—subsequent to January 1, 1942, you received an opinion of the attorney general in regard to this statute, did you not?

A. I did.

Q. And pursuant to that opinion you changed

(Testimony of Torkel Westly.)

your administrative practice in regard to the statute? A. We did.

Q. And when was that change made?

A. It was made as of January 1st, 1942.

Q. Did it affect contracts that had been entered into prior to January 1, 1942, but not to be performed until after January 1st, 1942?

A. No. We did exempt such contracts. Sales made on contracts entered into prior to January 1, 1942, to a very considerable extent, were exempt.

Q. Now these institutions which you have referred to as exempt will you please enumerate those.

A. You mean the public utilities?

Q. Yes, and the schools; with a brief description as to what they do. [94]

A. The public utilities are exempt from the gross income tax if that income is subject to the public utility tax.

Q. You take one public utility, for instance like the Honolulu Gas Company, they conduct quite a general retail business, in the general sense, do they not? A. Yes.

Q. It sells gas stoves, ranges and refrigerators and heaters and what not?

A. That is correct.

Q. And that concern pays a tax at what rate?

A. The Honolulu Gas Company does not pay any gross income tax.

Q. How about the sale of those goods?

A. The retail sales are included in the public utility tax. They pay a five per cent minimum pub-

(Testimony of Torkel Westly.)

lie utility tax on all of the gross income from the public utility business, which includes the retailing of stoves and ice boxes and so forth.

Q. Take another classification such as schools and hospitals, and charitable institutions; how are they treated?

A. They are tax exempt; they are exempt from the gross income tax, and sales to them are taxed at the retail rate to the seller.

Q. In other words, your treatment of Mr. Brodhead here is the same as you treat a person that sells to a charitable institution, is that right?

A. Exactly.

Q. And there is no discrimination between the firms? A. No discrimination of any kind.

Q. And it is the same as you would treat the seller who sells to a school cafeteria?

A. That is correct. [95]

Q. Are there some other classifications that are in that same category?

A. I cannot recollect.

Q. Well, what about sales to fraternal societies; benefit societies?

A. Oh, sales to benefit societies.

Q. Charitable corporations?

A. Yes. It depends on whether they are licensed under the gross income act; whether they are in business or not.

Q. Yes, but if they are a non-profit organization they would not be taxable under the gross income tax, would they?

(Testimony of Torkel Westly.)

A. That's right, and the tax paid, they would be taxed as a retail sale.

Q. That is, at $1\frac{1}{2}$ per cent?

A. Yes, as a retail sale, at $1\frac{1}{2}$ per cent.

Q. So you treat these activities on the same basis, do you not? A. Yes, that's right.

Q. Including the post exchanges?

A. Including the post exchanges.

Q. Now, suppose there is a sale to a public utility by a local taxpayer, what would that local taxpayer pay on his sale to the public utility?

A. He would pay $1\frac{1}{2}$ per cent if the public utility was subject to the utility tax on the resale.

Q. Suppose the particular item involved was an item which the public utility sold at retail in its store, would it still be $1\frac{1}{2}$ per cent?

A. The seller would still pay $1\frac{1}{2}$ per cent if that sale was subject to the public utility tax.

Q. Now you have mentioned the Honolulu Gas Company. What is [96] the practice with respect to the Hawaiian Electric Company? e

A. Well, the Honolulu Gas Company is 100 per cent; pays utility taxes on a 100 per cent basis, and the Hawaiian Electric is both utility and a non-utility business.

Q. Well, directing your attention to the utility end?

A. Well, in sales to the Hawaiian Electric which is included in the public utility business, whether it is resale—retail or wholesale, it is taxed to the seller at the retail rate.

(Testimony of Torkel Westly.)

Q. Of $11\frac{1}{2}$ per cent?

A. At $11\frac{1}{2}$ per cent, yes, because it is not for resale by the utility under the gross income act.

Q. In administering this law you are of course bound by the definition of what is a retailer and what is a wholesaler as defined in this statute?

A. That's right.

Q. What publicity did you give to the change of this administrative ruling in connection with this law, Mr. Westly?

A. We published one notice in the Honolulu Star-Bulletin for ten days, and another in the Advertiser—another one in the Honolulu Advertiser for ten days. The first date was December 31, 1941, and it ran consecutively for ten days.

Q. Is this a copy of the notice which you caused to have published in the Honolulu Star-Bulletin?

A. It is.

Mr. Anthony: We offer this in evidence, if the Court please.

The Court: Any objection.

Mr. Milton Cades: No objection.

The Court: It may be received and marked Defendant's Exhibit 1. [97]

The document offered in evidence is received and marked: Defendant's Exhibit 1.

(Testimony of Torkel Westley.)

DEFENDANT'S EXHIBIT No. 1

Notice to Gross Income Taxpayers

Effective January 2, 1942, All sales of tangible property made to the United States and/or its instrumentalities, departments or agencies (heretofore exempt), Must be included in the measure of the Gross Income Tax and Must be returned for taxable purposes under the Gross Income Tax Law of Hawaii. The foregoing shall not be construed as exempting sales of services or income derived from rents received from the United States and/or instrumentalities, departments or agencies prior to January 1, 1942.

All said sales as included in the measure of the tax shall be computed at the $11\frac{1}{2}\%$ rate, except in the case where a sale is made to a person (by "Person" is meant all entities coming within the meaning of said term as defined by the Gross Income Tax Law of Hawaii), reselling to the United States and/or its instrumentalities and/or its agencies. In cases of this nature, the first seller shall compute his taxable income at the $\frac{1}{4}$ of 1% rate, and the second seller (person selling to the United States and/or its instrumentalities and/or its agencies), shall compute his taxable income at the $11\frac{1}{2}\%$ rate.

Any person claiming that his gross income is taxable at the $\frac{1}{4}$ of 1% rate shall submit sufficient proof, as may be deemed necessary by this Depart-

(Testimony of Torkel Westly.)

ment, substantiating his claim to said rate of $\frac{1}{4}$ of 1%.

WM. BORTHWICK,
Tax Commissioner,
Territory of Hawaii.

FRANK ROSEHILL,
Deputy Tax Commissioner, Bureau of Gross In-
come and Consumption Taxes.

To: Honolulu Star-Bulletin, 10 days beg. Dec. 31,
1941.

To: Honolulu Advertiser, 10 days beg. Jan. 1,
1942.

[Notice of Publication of Notice to Gross
Income Taxpayers published in Honolulu Star-
Bulletin Dec. 31, 1941; Jan. 1, 2, 3, 5, 6, 7,
8, 9, 10, 1942; and Honolulu Advertiser Jan.
2, 3, 4, 5, 6, 7, 8, 9, 10, 11, 1942, attached.]

Filed C. C., June 16, 1943, R. P. Whitmarsh, Clerk
[Endorsed]: Filed Nov. 20, 1946.

Q. The opinion that you received from the attorney general which caused you to change the administrative practice in regard to this act was received prior to January 1, 1942, was it not?

A. It was.

Q. Mr. Westly, you testified, I believe, in regard

(Testimony of Torkel Westly.)

to the collection of the gross income tax from the Contractors? A. Yes.

Q. You refer to the P.N.A.B. Contractors, out here at Pearl Harbor? A. Yes, and others.

Q. That was the subject matter of a rather extensive litigation in the Federal Court, was it not? A. That is correct.

Q. And the conclusion of that litigation, the tax was paid on a compromise judgment, is that correct?

Mr. Russell Cades: I object to that, your Honor. The examination has only been as to the administrative practice, and has nothing to do with the particular case, otherwise we will go into collateral issues that will take a long time, and I object to this line of cross-examination; he is limited to the matter brought out on direct examination, and he has gone to great lengths, your Honor, to find out whether there is discrimination; we object to going into an independent inquiry on an utterly immaterial matter.

Mr. Anthony: This is touched on, on direct examination, and is also referred to in the stipulation. I don't care to pursue it any further, but this is just in line with the reason why the tax office made a change in their administrative practice. [98]

A. Yes.

Mr. Russell Cades: I move that the answer be stricken.

The Court: Do you want that out?

Mr. Russell Cades: I think your Honor, it just clutters up the record. If that answer is left in it

(Testimony of Torkel Westly.)

means pursuing the matter and getting into further questions. It is a different type of contract and a different type of problem.

The Court: I understand this is all they want on that cross-examination.

Miss Lewis: I would like to argue this motion if the court is going to entertain the motion.

The Court: All right.

Miss Lewis: It appears under the stipulation that during the period from January to June, 1942, as to which the plaintiff has asked for judgment to recover on the tax, we feel that we are not in court on it, nevertheless some statements were made about the P.N.A.B. Contractors, who were mentioned here. It probably appears that the tax commissioner had given the taxpayer the benefit of reducing the rate on the sales to the P.N.A.B. Contractors from $1\frac{1}{2}$ to $\frac{1}{4}$ of 1 per cent, and we wanted to show that the reason that was done was that the P.N.A.B. Contractors themselves are taxpayers. It is in line with the practice to which Mr. Westly has testified. We wanted to show that, although it appears in that stipulation, that rate has now been fixed at $\frac{1}{4}$ of 1 per cent by the tax commissioner, and it was done in accordance with his practice to which Mr. Westly has testified, and as to applying that rate if the person who buys is a taxpayer, and I think this is material to show that the P.N.A.B. Contractors are taxpayers. It explains the thing, and rounds out the whole picture here. If that fact is not explained the court [99] might afterwards, in

(Testimony of Torkel Westly.)

reviewing the case, wonder if there was an inconsistency in the practice in that regard, if that is raised. We have been very liberal in getting the whole picture before the court.

The Court: This may remain in. I take it there is nothing much further.

Q. And those Contractors are now paying the tax at the rate of $1\frac{1}{2}$ per cent?

Mr. Russell Cades: That is objected to.

A. They are.

Mr. Russell Cades: That is objected to, on the explanation—on the statement made by Mr. Westly, why only $\frac{1}{4}$ of 1 per cent was charged on sales to the P.N.A.B.

(Argument by Mr. Cades.)

(Argument by Mr. Anthony.)

(Argument by Mr. Cades.)

Mr. Russell Cades: I would like to renew my motion to strike the answer to the question that has just been asked.

Mr. Anthony: I have no desire to pursue this any further, your Honor.

(Argument by Miss Lewis on motion to strike.)

The Court: Are you making a motion?

Mr. Russell Cades: I am making a motion to strike the answer, your Honor. Whether it is clear or not, that is not material to the issue which is before your Honor.

(Testimony of Torkel Westly.)

The Court: You are really making a motion to strike in order to be in a position to object to the question, isn't that right? It is just something that occurs repeatedly in trial courts.

Mr. Russell Cades: That is correct. [100]

The Court: The motion to strike is granted, in order that you may object to the question. And you do object to the question?

Mr. Russell Cades: Then I object to the question.

The Court: The objection is sustained, because it was stated that, after the last question, the matter would not be pursued any farther.

Q. Did the Contractors, P.N.A.B. pay taxes for the period January to June, 1942? A. Yes.

Q. At what rate? A. 1½ per cent.

The Court: The P.N.A.B. is what?

Mr. Anthony: Pacific Naval Air Bases, Contractors—or Contractors, Pacific Naval Air Bases.

Mr. Milton Cades: I don't see how that last question has any bearing on the issue here, and I have a motion to strike.

The Court: There was enough time to object, if you felt it necessary, and that time has passed; no objection was made. The question has been answered.

Mr. Milton Cades: We move to strike the answer so as to present our objection.

The Court: I watched very carefully to see if there would be any objection to that question. I

(Testimony of Torkel Westly.)

thought there might be. There wasn't any and the witness answered.

Mr. Milton Cades: Well, your Honor, we were distracted for a moment or we would have objected more promptly. There was a note passed here, if your Honor please, in this connection, in regard to something about this Contractors, P.N.A.B.

Mr. Anthony: What is there before this Court?

Mr. Milton Cades: There is a motion to strike.

The Court: I think you are assuming that you made a motion. I don't remember. Did you really make a motion?

Mr. Milton Cades: I made a motion, if your Honor please.

The Court: May I make another suggestion, gentlemen. It often is required that on any examination only one attorney on each side be heard, because otherwise we get confused. We look to one attorney, when maybe the other attorney is really moving, so with this particular witness for the plaintiff it should be either Mr. Russell Cades or Mr. Milton Cades, and for the defendant either the Attorney General or Miss Lewis. It makes it very difficult for the court to rule, and hard on the reporter. I think you wanted to make a motion to strike, did you not?

Mr. Milton Cades: Yes.

Mr. Anthony: I have no further questions, your Honor.

Mr. Milton Cades: In connection with the motion to strike, the whole testimony with regard to

(Testimony of Torkel Westly.)

the Contractors, P.N.A.B. appears to be based on the fact that the United States by its Attorney General or general counsel has sanctioned the payment of tax to the Territory. Actually, as I recall, and I may be wrong, the stipulation contains a statement that the whole matter is a matter of compromise, and that none of the facts admitted in there are to be taken or used for any other purpose and that the conclusions are not binding on any of the parties for any other purpose except for the purpose of compromise, so that any question as to the payment of the tax by any particular contractor I believe is utterly irrelevant to this matter.

The Court: The statement has been made that the [102] subject will not be pursued any further. The motion to strike is denied.

Mr. Milton Cades: May I take an exception.

The Court: Certainly. The court will take its usual recess for 10 minutes.

(A recess was here taken.)

Mr. Anthony: We rest, your Honor.

Mr. Milton Cades: We have no further evidence to offer. We rest.

(A discussion was held between Court and counsel with respect to the filing of memorandums.)

The Court: Shall we fix it at 15 days, 15 days and 10?

Mr. Milton Cades: Yes, that's right.

Mr. Anthony: Yes, your Honor.

The Court: So ordered.

Case Closed

I Hereby Certify the above and foregoing, pages 1 to 30, inclusive, to be a full, true and correct transcript of my shorthand notes taken in the within-entitled matter at the time and place therein stated.

Honolulu, T. H., March 30, 1944.

/s/ R. N. LINN,

Official Reporter.

[Endorsed]: Filed April 27, 1944. [103]

In the Supreme Court of the Territory of **Hawaii**

No. 2631

THOMAS H. BRODHEAD,

d.b.a. T. H. Brodhead Co.,

Plaintiff,

Plaintiff-in-Error,

vs.

WILLIAM BORTHWICK, Tax Commissioner of
the Territory of Hawaii,

Defendant,

Defendant-in-Error.

Action to Recover Gross Income Taxes

Paid Under Protest

Error to Circuit Court, First Judicial Circuit
Honorable A. M. Christy, Second Judge, Presiding

The Territory of Hawaii: To the Clerk of the Circuit Court, First Judicial Circuit, Territory of Hawaii:

Witness the Honorable S. B. Kemp, Chief Justice of the Supreme Court of the Territory of Hawaii, this 7th day of August, 1946.

Return to Writ of Error

The execution of the within writ of error appears by the record hereto annexed.

Dated at Honolulu, T. H., this 16th day of November, 1946.

[Seal] /s/ B. GRIEP,
 Clerk of the Circuit Court of
 the First Judicial Circuit.

[Endorsed]: Filed Aug. 7, 1946. [107]

[Title of Supreme Court and Cause.]

ASSIGNMENT OF ERRORS

Comes now Thomas H. Brodhead, doing business as T. H. Brodhead Co., plaintiff-in-error above named, and petitioner for writ of error in the above entitled cause and presents this assignment of errors and says that in the record and proceedings in the above entitled cause, and in the judgment made and entered therein on May 15, 1946, there are manifest and prejudicial errors in the particulars hereinafter set forth, to wit:

Assignment No. 1

The Court erred in making and entering judgment for the defendant (defendant-in-error herein) for the reason that said judgment was contrary to the law, contrary to the evidence and contrary to the weight of the evidence, which judgment was duly excepted to by the defendant.

Assignment No. 2

The Court erred in making and rendering its decision dated May 15, 1946, in that the same was contrary to the law, contrary to the evidence and contrary to the weight of the evidence, which decision was duly excepted to by the defendant. [109]

Assignment No. 3

The Court erred in holding that the General Excise Tax Law of the Territory of Hawaii (Act 141, Series A44, Sessions Laws of Hawaii 1935, as amended) herein referred to as the Excise Tax Law,

imposes a tax and, for the period from October 1, 1942, through March 31, 1944, did impose a tax upon the plaintiff with respect to sales of tangible personal property made to the United States government, its departments and agencies.

Assignment No. 4

The Court erred in holding that Section 3 of said laws did not exempt the plaintiff from tax on the gross proceeds of sales made by him to the United States Government and its Post Exchanges and Ships' Service Stores.

Assignment No. 5

The Court erred in failing to hold that the Legislature in enacting said Excise Tax Law intended to exempt from taxation the proceeds of sales to the United States, its departments and agencies.

Assignment No. 6

The Court erred in holding that the tax as so imposed does not levy a burden upon or interfere with Federal activities.

Assignment No. 7

The Court erred in failing to hold that said Excise Tax Law so administered as to include the gross receipts from sales to the United States, its agencies or instrumentalities, within the measure of tax on the United States which is within the prohibition of the rule against the taxation of a sovereign.

Assignment No. 8

The Court erred in failing to hold that the tax as so imposed is a direct burden on the Federal government in the exercise of its essential governmental power of raising and supporting [110] armies and of providing and maintaining a Navy, and that said tax therefore violates Article I, Section 8, Clauses 12 and 13 of the Constitution of the United States.

Assignment No. 9

The Court erred in holding that such tax had only an economic effect upon the United States Government, its departments and agencies, which economic effect is indirect and does not constitute the tax an invalid burden upon or interference with Federal activities.

Assignment No. 10

The Court erred in holding that the imposition of said tax was and is within the power of the Legislature of the Territory under Section 55 of the Hawaiian Organic Act and not in violation of Article I, Section 8, Clause 12 or 13, or the Fifth Amendment of the Constitution of the United States.

Assignment No. 11

The Court erred in failing to hold that said tax violates the Fifth Amendment of the Constitution of the United States in that it constitutes a tax on the privilege of doing business with the United States, its agencies or instrumentalities.

Assignment No. 12

The Court erred in holding that said tax did not violate Section 55 of the Hawaiian Organic Act in that it imposes a direct tax on the privilege of doing business with the United States which is a subject beyond the legislative power of the Legislature of the Territory of Hawaii, in that it is not a rightful subject of legislation and in that it is inconsistent with the Constitution and laws of the United States.

Assignment No. 13

The Court erred in holding that the rate of tax imposed by said General Excise Tax Law upon all gross proceeds of [111] sales to the Federal Government and agencies thereof was at the rate of $1\frac{1}{2}\%$ irrespective of whether such goods were intended to be or were resold by the purchasers.

Assignment No. 14

The Court erred in holding that the tax imposed by said law upon the gross proceeds of sales to United States Post Exchanges and Ships' Service Stores for the purpose of resale was at a rate higher than $\frac{1}{4}$ of 1%.

Assignment No. 15

The Court erred in holding that a tax on sales to Post Exchanges and Ships' Service Stores at a higher rate than on sales to other retailers is not prohibited as an indirect way of doing what cannot be done directly under the Constitution of the United States.

Assignment No. 16

The Court erred in holding that said tax law required the Tax Commissioner to include in the measure of tax the proceeds of sales to the United States and its agencies at the rate of $1\frac{1}{2}\%$.

Assignment No. 17

The Court erred in holding that the administrative practice, whereby the rate of tax on sales to Post Exchanges and Ships' Service Stores was increased because of a judicial determination that Post Exchanges and Ships' Service Stores could not be constitutionally taxed on their sales, did not show that the purpose of the administrators was to accomplish an unlawful result by an indirect method.

Assignment No. 18

The Court erred in holding that the classifications made by the Legislature are "natural and reasonable and not discriminatory" against the plaintiff or the Federal government or its instrumentalities.

Assignment No. 19

The Court erred in holding that Post Exchanges and Ships' Service Stores are not "merchants" within the meaning of the tax law.

Assignment No. 20

The Court erred in holding that a tax upon plaintiff at a higher rate on account of its sales to Ships' Service Stores and Post Exchanges for resale than upon its sales to licensed retailers for resale was

not discriminatory against the plaintiff or the Federal government or its instrumentalities.

Assignment No. 21

The Court erred in holding that the Tax Commissioner did not discriminate in the administration of the tax law against the plaintiff or the Federal government or its instrumentalities.

Assignment No. 22

The Court erred in holding in the Decision and Judgment made and entered in this cause that the plaintiff is not entitled to recover the gross income taxes paid by him under protest or any part thereof for the reason that the Legislature specifically exempted such gross proceeds of sales from the tax law; for the further reason that the Legislature is without power to impose a tax upon the proceeds of gross sales to the United States or its instrumentalities; and for the further reason that in no event can the Legislature impose a tax upon the gross proceeds of sales to Ships' Service Stores and Post Exchanges for resale at a higher rate than that imposed on account of sales to other retailers for resale, namely $\frac{1}{4}$ of 1%.

Assignment No. 23

The Court erred in failing to make a Judgment in favor of the plaintiff that he recover gross income taxes paid under protest in accordance with his prayer as set forth in the complaint.

Wherefore, plaintiff-in-error and petitioner for writ of [113] error prays that the Judgment made

and entered in the above entitled cause on May 15, 1946, be reversed and for such other and further relief as may be proper.

Dated, Honolulu, T. H., this 7th day of August, 1946.

SMITH, WILD, BEEBE &
CADES,

By /s/ MILTON CADES,
Attorneys for plaintiff,
plaintiff-in-error.

[Endorsed]: Filed Aug. 7, 1946. [114]

[Title of Supreme Court and Cause.]

STIPULATION

It Is Hereby Stipulated by and between the parties to the above entitled cause, through their respective counsel, that the points raised by the assignment of errors of the plaintiff-in-error, filed August 7, 1946, be and they hereby are submitted for the decision of the Court upon the arguments made by the respective parties in their briefs filed in this Court in Supreme Court No. 2583, and without oral argument.

Dated at Honolulu, T. H., February 24, 1947.

SMITH, WILD, BEEBE &
CADES,

By /s/ MILTON CADES,
Attorneys for Plaintiff,
Plaintiff-in-Error.

/s/ RHODA V. LEWIS,
Assistant Attorney General,
Attorney for Defendant,
Defendant-in-Error.

Approved:

/s/ S. B. KEMP,
Chief Justice,
Supreme Court of the
Territory of Hawaii.

[Endorsed]: Filed Feb. 24, 1947. [116]

In the Supreme Court of the Territory of Hawaii

October Term 1946

No. 2631

THOMAS H. BRODHEAD

vs.

WILLIAM BORTHWICK, Tax Commissioner of
the Territory of Hawaii.

Error to Circuit Court First Circuit

Hon. A. M. Christy, Judge.

Submitted February 24, 1947. Decided February
25, 1947.

Kemp, C. J., Peters and Le Baron, JJ.

DECISION

Per Curiam. This is a writ of error to review a judgment of the circuit court in an action, tried jury waived, which was brought by the plaintiff-plaintiff in error, under the provisions of section 1575, Revised Laws of Hawaii 1945 (formerly section 571, Revised Laws of Hawaii 1935) to recover taxes paid under protest. The court rendered its decision and judgment in favor of the defendant on May 15, 1946, and the case comes here on plaintiff's

writ of error. This case was previously before the court as No. 2583, on a writ of error filed by the defendant to review a decision and judgment of the circuit court in favor of the plaintiff. This court, by a decision rendered March 4, 1946, denied the plaintiff's petition for rehearing. The previous decision was rendered by a majority of two judges. Mr. Justice Le Baron [118] concurring in part and dissenting in part. The decision and judgment now brought before this court was rendered on the new trial pursuant to the remand of the case in number 2583. Another case, number 2581, which was consolidated for briefing and argument with number 2583 and also remanded for a new trial, is not now before this court.

The parties, by stipulation, have submitted the points raised by the plaintiff's assignment of errors, now before the court, upon the arguments made by the respective parties in their briefs filed in this court in number 2583, and without oral argument. The majority of the court, Chief Justice Kemp and Mr. Justice Peters, are of the same opinion as when this case was heard before, and the dissenting judge, Mr. Justice Le Baron, also is of the same opinion. On the reasoning stated in the opinion of the court, rendered March 4, 1946 (37 Haw. 314), and in the decision denying rehearing on March 27, 1946 (37 Haw. 351), the court holds that the assignment of errors in this case is without merit and accordingly the judgment of the circuit court, Honorable A. M. Christy, Judge, is affirmed. A judgment

is accordance with this decision will be entered upon presentation.

By the Court:

/s/ GUS K. SPROAT,
Clerk.

Smith, Wild, Beebe & Cades for plaintiff-plaintiff
in error.

Rhoda V. Lewis, Assistant Attorney General, for
defendant-defendant in error. [119]

Approved:

/s/ S. B. KEMP,
Chief Justice.

/s/ E. C. PETERS,
Associate Justice.

/s/ LOUIS LE BARON,
Associate Justice.

Approved as to form:

SMITH, WILD, BEEBE &
CADES,

By /s/ MILTON CADES,
Attorneys for plaintiff-
plaintiff-in-error.

/s/ RHODA V. LEWIS,
Assistant Attorney General,
Attorney for defendant,
defendant-in-error.

[Endorsed]: Filed Feb. 25, 1947. [120]

In the Supreme Court of the Territory of Hawaii

No. 2631

THOMAS H. BRODHEAD,

d.b.a. T. H. Brodhead Co.,

Plaintiff,

Plaintiff-in-Error,

vs.

WILLIAM BORTHWICK, Tax Commissioner of
the Territory of Hawaii,

Defendant,

Defendant-in-Error.

Action to Recover Gross Income Taxes
Paid Under Protest

Error to Circuit Court, First Judicial Circuit
Honorable A. M. Christy, Second Judge, Presiding

JUDGMENT

Pursuant to the written decision of this Court,
filed herein on February 25, 1947,

It Is the Judgment of This Court that for the
reasons set forth in said decision, the judgment of
the Circuit Court that the plaintiff take nothing by

his complaint and dismissing the action, be and it hereby is affirmed.

Dated at Honolulu, T. H., February 25, 1947.

By the Court:

[Seal] /s/ GUS K. SPROAT,
Clerk.

Approved:

/s/ S. B. KEMP,
Chief Justice,
Supreme Court of the
Territory of Hawaii.

Approved as to form:

SMITH, WILD, BEEBE &
CADES,

By /s/ MILTON CADES,
Attorneys for Plaintiff,
Plaintiff-in-Error.

[Endorsed]: Filed Feb. 25, 1947. [122]

In the Supreme Court of the Territory of Hawaii,

October Term, 1945

THOMAS H. BRODHEAD

vs.

WILLIAM BORTHWICK, Tax Commissioner of
the Territory of Hawaii.

Nos. 2581 and 2583

Error to Circuit Court First Circuit

Hon. J. A. Matthewman, Judge

Argued November 19, 20, 1945.

Decided March 4, 1946

Kemp, C. J., Peters and Le Baron, JJ.

Territories—legislative power—taxation.

The legislature of the Territory is empowered to lay an excise tax upon all businesses and activities carried on in the Territory measured by the application of rates against values, gross proceeds of sales or gross income, as the case may be.

Licenses—for occupations and privileges—constitutionality and validity.

Such a tax is not within the implied constitutional prohibition against laying a burden upon or interfering with federal activities merely because in its incidence it might indirectly reach a federal instrumentality.

Id.—id.

The general excise tax law of 1935 is valid although in [124] its incidence it indirectly affects the United States Government and its departments or agencies.

Id.—id.—subjects of license or tax—wholesalers.

Where the tax upon sales of tangible personal property is applicable generally to “every person engaged or continuing in the business of selling” the same, from whom is excepted wholesalers, sales not coming within the statutory definition of “wholesalers,” are subject to the rate of tax applicable to “every person” and not to the rate of tax applicable to wholesalers.

Tax—constitutional requirements and restrictions—discrimination.

The legislature may classify objects for the purpose of taxation. Diversity of rate of taxation based upon proper classification of the objects of taxation is not discrimination.

OPINION OF THE COURT BY PETERS, J.

(Le Baron, J., concurring in part and dissenting in part.)

The opinion of Mr. Justice LeBaron renders a statement of the case and of the errors relied upon unnecessary. It will suffice to state our conclusions.

As we view the case, the extension by section 55 of the Organic Act of the legislative power of the

Territory to all rightful subjects of legislation not inconsistent with the Constitution and laws of the United States, locally applicable, includes the power to lay, consistently with the restriction and limitations imposed by the Constitution and laws of the United States, an annual excise tax upon all businesses and activities carried on in the Territory measured by the application of rates against values, gross proceeds of sales or gross income, as the case might be.¹ A tax imposed by a nonfederal political agency, however reasonable, universal and nondiscriminating, the legal effect of which is to lay a direct and immediate tax upon the instrumentalities of the United States, is within the implied prohibition of the Constitution of the United States against laying a burden upon or interfering with federal activities,² even though imposed under the guise of an excise tax.³ A nondiscriminating territorial excise tax measured by the application of rates against values, gross proceeds of sales or gross income, as the case may be, is not within the constitutional pro-

¹*W. C. Peacock & Co. v. Pratt*, 121 Fed. 772; *Haavik v. Alaska Packers Assn.*, 263 U. S. 510, 513; *Kitagawa v. Shipman*, 54 F. (2d) 313, 318; *Yerian v. Territory of Hawaii*, 130 F. (2d) 786, 788; *Robertson v. Pratt*, 13 Haw. 590.

²*Johnson v. Maryland*, 254 U. S. 51, 55; *Mayo v. United States*, 319 U. S. 441.

³*Choctaw & Gulf R. R. v. Harrison*, 235 U. S. 292; *Northwestern Ins. Co. v. Wisconsin*, 275 U. S. 136; *Panhandle Oil Co. v. Knox*, 277 U. S. 218; *Macallen Co. v. Massachusetts*, 279 U. S. 620.

hibition merely because in its incidence it might indirectly [126] reach a federal instrumentality.⁴ It was the intention of the legislature, as manifested by sections 2, 24 and 3 of the general excise tax law of 1935, that in the computation of the tax there be excepted from gross proceeds of sales or gross income only so much of the gross proceeds of sales or gross income derived from the sales made to the United States Government, its departments or agencies, which was then or might thereafter be exempted from taxation under the Constitution of the United States or the Organic Act of the Territory, such exception, however, not to apply if and when the Congress of the United States permitted the Territory to impose a privilege tax upon gross proceeds of sales made to the United States Government, its departments or agencies. And although in its incidence the local general excise tax law of 1935⁵ indirectly affects the United States Government and its departments or agencies, its economic

⁴*Society for Savings v. Coite*, 6 Wall. 594 (1867); *Home Ins. Co. v. New York*, 134 U. S. 594 (1889); *Provident Institution v. Massachusetts*, 6 Wall. 611 (1867); *Hamilton Company v. Massachusetts*, 6 Wall. 632 (1867); *Metcalf & Eddy v. Mitchell*, 269 U. S. 514 (1925); *Fidelity & Deposit Co. v. Pennsylvania*, 240 U. S. 319 (1915); *Trinityfarm Co. v. Grosjean*, 291 U. S. 466 (1933); *James v. Dravo Contracting Co.*, 302 U. S. 134 (1937); *Alabama v. King & Boozer*, 314 U. S. 1 (1941); *Curry v. United States*, 314 U. S. 14 (1941).

⁵Sess. Laws 1935, Act 141.

effect is consequential and remote and not immediate and direct.⁶

Whether or not the effect of the decision in the case of *Panhandle Oil Co. v. Knox* was to extend constitutional immunity from taxation under the local excise law to the gross proceeds of sales to federal instrumentalities is deemed of no importance further than it may serve to ascertain the legislative [127] intent in the use of the language contained in section 3 of the Act. Nor whether the *King & Boozer* case overruled the *Panhandle Oil Co.* case. The tax, the legality of which is in question herein, was assessed for the year 1942. The *King & Boozer* case was decided in November, 1941. And the rationale of the *King & Boozer* case applies⁷ without the necessity of further legislation on the subject.⁸ Nor are we concerned with the question of whether the legislature was correct in assuming, as indicated by the proviso of section 3, that the Congress of the United States is authorized to permit the Territory to impose a privilege tax upon gross proceeds or gross income derived from sales made to the United States Government, its depart-

⁶*Alabama v. King & Boozer*, *supra*. See also dissenting opinion of Mr. Justice Holmes in *Panhandle Oil Co. v. Knox*, *supra*, dissenting opinion of Mr. Justice Stone in *Macallen Co. v. Massachusetts*, *supra*; *Trinityfarm Co. v. Grosjean*, *supra*.

⁷*Philadelphia v. Schaller*, 148 Pa. Super. Ct. 276, 25 A. (2d) 406, cert. denied 317 U. S. 649.

⁸*Western L. Co. v. State Bd. of Equalization*, 11 Cal. (2d) 156, 78 P. (2d) 731.

ments or agencies or that it was legally necessary to do so. An intent clearly and unequivocally expressed is no less so because it may be based upon a false hypothesis.

The only troublesome question involved is whether the rate to be applied to gross proceeds of sales or gross income, as the case might be, should be one and one-half per cent, the rate applicable to "every person engaging or continuing * * * in the business of selling any tangible personal property whatsoever (not including, however, bonds or other evidence of indebtedness or stocks)" or the rate of one [128] quarter of one per cent, the rate applicable "in the case of a wholesaler or producer."

Section 2, B (1) of the Act imposes a tax "Upon every person engaging or continuing within this Territory in the business of selling any tangible personal property whatsoever (not including, however, bonds or other evidence of indebtedness or stocks)" of one and one quarter per cent (since increased to one and one-half per cent) of the gross proceeds of sales of the business, except in the case of wholesalers or producers, in which case it is one quarter of one per cent. Section 1, paragraph (8) defines "gross proceeds of sale" as the "value actually proceeding from the sale of tangible personal property without any deduction on account of the cost of property sold or expenses of any kind." Section 1, paragraph (10) defines a wholesaler as "a person doing a regularly organized wholesale or jobbing business, known to the trade as such, and only with respect to the following sales: (a) sales, to a licensed

retail merchant or jobber, for purposes of resale; (b) sales, to a licensed manufacturer, of material or commodities which are to be incorporated by such manufacturer into a finished or saleable product (including the container or package in which the product is contained) during the course of its preservation, manufacture or processing, including preparation for market, and which will remain in such finished or saleable product in such form as to be perceptible to the senses, which finished saleable product is to be sold and not otherwise used by such manufacturer; or (c) sales, to a licensed contractor, of material or commodities which are to be incorporated by such [129] contractor into the finished work or project required by the contract and which will remain in such finished work or project in such form as to be perceptible to the senses." It is apparent from the foregoing references to the Act that the legislature intended that the rate of tax applicable to the gross proceeds of all sales of tangible personal property should be one and one-quarter per cent or such rate to which the same might be decreased or increased under the provisions of section 2, III, except in the cases of sales made by a wholesaler as defined and in respect to the types of sales enumerated and defined in section 1, paragraph (10) (a), (b) or (c), and except in case of sales made by a producer, when the rate should be one quarter of one per cent. Whether or not, after excluding wholesalers or producers from the all-inclusive phrase "upon every person," retailers alone remain is a question that is not involved. The

Act, besides carrying its own definition of a "wholesaler" and the sales to which the term shall apply, thus restricting and limiting the ordinarily accepted meaning of the term "wholesaler," also carries a definition of the term "retailer" [§ 1, par. (13)] and of the term "producer" [§ 1, par. (11)]. Unquestionably, the phrase "upon every person" includes retailers, and this conclusion is confirmed by the running head of section 1, B, and the administrative regulations in respect to retailers contained in section 2, 1-B (1), (3), (4) and (5).

It is conceded that the tax in question involves sales of tangible personal property, not including bonds or other evidence of indebtedness or stocks. Hence, the gross proceeds of sales made by the taxpayer of tangible personal [130] property was subject to a tax of one and one-quarter per cent unless, as claimed by him, they were made by him as a wholesaler and come within any of the categories of sales defined in section 1, paragraph (10) (a), (b) or (c). The taxpayer claims that the sales made to post exchanges and ships' service stores come within section 1, paragraph (10) (a). It is admitted by the Territory that the taxpayer does a regularly organized wholesale business, known to the trade as such, and that the sales involved were for the purpose of resale. But are post exchanges and ships' service stores "licensed merchants," as that term is used in section 1, paragraph (10) (a)? We think not. Post exchanges and ships' stores are admittedly federal instrumentalities. While post exchanges and ships' stores sell at "retail" and the sales in question were

made for purpose of resale, neither post exchanges nor ships' stores are "licensed," as that term is used in section 1, (10) (a). By section 21 of the Act all persons having gross proceeds of sales upon which a privilege tax is imposed by the Act are required, as a condition precedent to engaging or continuing such business, to secure an annual license upon conditions that are immaterial to our discussion. It is therein further provided that: "Any person who may lawfully be required by the Territory, and who is required by this Act, to secure a license as a condition precedent to engaging or continuing in any business subject to taxation under this Act, who shall engage or continue in such business without securing such license in conformity with this Act, shall be guilty of a misdemeanor * * *." A privilege tax is not imposed by the Act upon the gross proceeds of sales by federal instrumentalities. While [131] not expressly exempted, they are, as heretofore pointed out, immune from such taxation by the Territory. Hence, one of the essential attributes of a "licensed merchant" is absent and the legal effect is to exclude such sales from the category of sales defined in section 1, paragraph (10) (a). In other words, in respect to sales to federal instrumentalities, the taxpayer was not a wholesaler as defined in the Act.

In our opinion the word "licensed" included in the definition of sales in section 1, paragraph (10) (a), was used by the legislature advisedly. It must be assumed that it was advised of the immunity from taxation of federal instrumentalities. It extended

exemptions by the Act itself to certain business activities exercising retail functions, viz., hospitals, infirmaries and sanatoria. It no doubt had in mind other business activities which, though retailers in a popular sense, nevertheless legally were not retailers under the terms of the Act. In each of the instances referred to no license is required under the provisions of section 21 of the Act. From all this it is abundantly clear that by the use of the word "licensed" the legislature intended to exclude from the definition of "wholesaler" sales made to persons exercising retail functions who under the provisions of the Act were not required to be licensed.

Nor are we satisfied that post exchanges and ships' service stores are "merchants" in the sense that the term "merchant" is employed in section 1, paragraph (10) (a). The Act itself does not define the word "merchant." Hence, its common-law meaning controls. A merchant has been defined as [132] one who is engaged in buying and selling goods, wares or merchandise for gain or profit.⁹ The army regulations governing post exchanges are in evidence. It was stipulated that ships' service stores have the same relation to the United States Navy as post exchanges have to the United States Army. The regulations governing post exchanges are epitomized in the opinion of the court in the case of

⁹Bacon v. Cannady, 144 Ga. 293, 86 S. E. 1083; In re Jupp, 274 Fed. 494; Rosenbaum v. City of Newbern, 118 N. C. 83, 24 S. E. 1; H. H. Kohlsaat & Co. v. O'Connell, 255 Ill. 271, 99 N. E. 689.

Standard Oil Co. v. Johnson, 316 U. S. 481, at 484. It was there held: “* * * post exchanges as now operated are arms of the Government deemed by it essential for the performance of governmental functions. They are integral parts of the War Department, share in fulfilling the duties entrusted to it.” If post exchanges and ships’ service stores as now operated are arms of the Government and integral parts of the respective services to which they are attached, their functions are governmental and not proprietary,¹⁰ and in whomever the title to the tangible personal property sold may be vested immediately prior to sale, such person is not a “merchant” within the meaning of section 1, paragraph (10) (a) of the Act. For this additional reason the taxpayer was not a wholesaler as defined in the Act.

Nor does the imposition of the higher rate of taxation applicable to “every person” juridically discriminate against sales to federal instrumentalities.

The term “retailer” is defined in the Act as “any person who sells, other than as a wholesaler within the definition of this Act, tangible personal property for consumption or use by the purchaser and not for resale.” The statutory [133] definition of the word “wholesaler” has already been quoted. If, as heretofore held, the taxpayer is not a “wholesaler” as defined by the Act and is included in the all-inclusive term of “every person” employed in section 2,

¹⁰Fed. Land Bank v. Bismark Co., 314 U. S. 95, 102.

B, which levies the tax, he is simply one of a class to which the rate imposed uniformly applies. "Every person" selling to federal instrumentalities pays the same tax. All vendors of the same class are treated alike. Moreover, by the same token, sales to retailers are divided into two classes, viz., (1) sales to a retailer either not licensed or not a merchant, when the vendor falls into the category of "every person" and the higher rate applies, and (2) sales "to a licensed retail merchant for purposes of resale" when the vendor falls into the excepted class of "wholesaler" and the lower rate applies. In either case all vendors in the respective classes to which they belong are treated uniformly and pay the same applicable tax.

The exception of "wholesalers" as a class from "every person" as a class affects a natural and reasonable classification of vendors especially where, as here, it synchronizes with the evident intent of the legislature, speaking generally, that sales of tangible personal property in their normal distribution through commercial channels bear two taxes, viz., one when sold at wholesale when the rate is one-quarter of one per cent and one when sold at retail when the rate is one and one-half per cent. The same may be said of the classification of sales to retailers where resales by the retailers are non-taxable by reason of immunity, exemption or otherwise. They are readily distinguishable from sales to a "licensed retail merchant." And the legislature [134] apparently intended that as to each class a different rate of taxation obtain, in the former the

rate of one and one-half per cent as sales made by "every person" and in the latter one-quarter per cent as sales made by a "wholesaler." The well-settled rule that the legislature may classify objects for the purposes of taxation has long since received recognition and been applied by this court.¹¹ Diversity of rate of taxation based upon proper classification of the objects of taxation is not discrimination. It would serve no useful purpose to pedantically repeat what this court has heretofore said on the subject. The language of the court in the Robertson case and the authorities there cited are equally applicable here.

Moreover, factually no discrimination exists against sales to post exchanges or ships' service stores. If anything, it is the other way about. And of this plaintiff does not complain.

It has been tritely said that the ultimate consumer always pays the tax. Here it is a question of the absorption of the tax by the retailer. The post exchanges and ships' service stores, however, by reason of their immunity, absorb less in taxes under the general excise tax law of 1935 than licensed retail merchants. In the former case the tax to be absorbed is only one and one-half per cent, in the latter one and three-fourths per cent. The result is that the purchasers to whom sales at post exchanges and ships' service stores are restricted as ultimate consumers pay less [135] than the general public purchasing from licensed retail merchants.

¹¹Naone v. Thurston, 1 Haw. 392; Campbell v. Shaw, 11 Haw. 112; Robertson v. Pratt, *supra*.

The judgment appealed from is reversed and the cause remanded for a new trial.

R. V. Lewis, Assistant Attorney General (also on the briefs) for Tax Commissioner, defendant-plaintiff in error.

M. Cades (Smith, Wild, Beebe & Cades on the brief) for plaintiff-defendant in error.

/s/ S. B. KEMP,

/s/ E. C. PETERS. [136]

OPINION OF LE BARON, J.

(Concurring in part and dissenting in part)

The defendant in error, hereinafter referred to as the taxpayer, under protest paid two privilege taxes to the Territory of Hawaii, pursuant to the "General Excise Tax Law" popularly known as the "Gross Income Tax Act." (Act 141, S. L. 1935, as amended, now §§ 5441-5482, R. L. H. 1945.) One tax was levied and collected by the plaintiff in error, hereinafter referred to as the tax commissioner, upon the taxpayer's gross proceeds of or income derived from sales, made for the use and consumption of various federal departments, to the United States and the other was likewise levied and collected upon those of or derived from sales, made for purposes of resale, to post exchanges of the Army and ships' services of the Navy of the United States. For convenience both sets of sales are referred to collectively as "federal sales" and the

taxes with respect to them as the "tax," except as the context hereof may otherwise require. They were made and collected respectively for a period beginning July 1, 1942, and ending March 31, 1944.

The taxpayer brought appropriate action to recover the tax. After trial, jury waived, the trial judge found no legislative intent in the Act to impose taxation upon gross proceeds of or gross income derived from federal sales and rendered judgments accordingly for full recovery of the tax paid. From these judgments the tax commissioner sued out writs of error which have been consolidated for hearing and argument before this court.

Four main questions are posited on appeal. Did the legislature intend to impose taxation upon gross proceeds of or gross income derived from federal sales? If it did, is its imposition valid? If the imposition is valid, then is the rate at which the tax was assessed relative to sales, made for the purposes of resale, to post exchanges and ships' services authorized by the legislature, the taxpayer not protesting the rate assessed relative to sales, made for use and consumption, to the United States? If authorized, is that assessment valid?

In section 2, subsection 1, of the Act, the legislature imposes privilege taxes upon "the persons on account of their business and other activities in this Territory," thereby plainly identifying the persons taxable under the Act and clearly explaining why they are taxable without any limitation whatsoever respecting the character of persons with whom they may deal or the nature of the business of such other

persons. This imposition of tax embraces "every person engaging or continuing within this Territory in * * * business" or other activity as designated and set forth by the paragraphs immediately thereunder. The legislative intent therein manifested is consonant with the general purpose of the Act to exercise the legislative tax power of the Territory to the full extent permitted by the Organic Act of the Territory and the Constitution of the United States, such purpose being indicated by its general severability clause and special provision directed against any unconstitutional taxation upon gross proceeds of sales derived from sales made to the United States, its departments or agencies. (§§ 24 and 3, *supra*.) In the general severability clause the legislature contemplates the possibility that some portions of the Act after its enactment would be declared invalid and provides against the impairing of the remaining portions by reason of such a declaration, expressly stating that "If the application of any provision of this Act to any person or circumstances is held invalid, the [138] application of such provision to other persons or circumstances shall not be affected thereby." (§ 24, *supra*.) In the specific provision relative to unconstitutional taxation, the legislature, pertinent to the case of the taxpayer, provides that: "In computing the amounts of any tax imposed under this Act, there shall be excepted from the gross proceeds of sales * * * so much thereof as * * * is derived from any sales made to the United States government, its departments or agencies, which is, or may here-

after be, exempted * * * under the Constitution of the United States or the Organic Act of the Territory * * *.” (§ 3, *supra*.) Post exchanges and ships’ services of the Army and Navy undisputedly come within the term “its departments or agencies” and sales to them as well as to the United States likewise come within the term “federal sales” as used in this opinion. (See *Standard Oil Co. v. Johnson*, 316 U. S. 481, 86 L. Ed. 1161.) While such specific exclusion may not have been necessary in view of the comprehensive nature of the severability clause, it manifests a caution by the legislature which in no way detracts from the force of the plain, certain and unambiguous language employed. A bare reading of it as well as of the Act as a whole suffices to demonstrate that all gross proceeds of sales capable of being taxed by the Territory under the Constitution or Organic Act are clearly within the scope of taxation intended by the legislature.

Consequently, the first basic issue to be determined relative to whether gross proceeds of federal sales are within the scope of the Act is whether they at the time of receipt and levy were in fact precluded therefrom by the Constitution of the United States by reason of an exemption from taxation therein, the parties being agreed that the meaning of the [139] Constitution in respect to such an exception must be found in the decisions of the Supreme Court of the United States.

In considering such decisions, it is evident that the Supreme Court of the United States had adopted, prior to the Act’s effective date of July 1,

1925, a construction of the Federal Constitution exempting federal sales from any taxation by a State without regard to whether the tax is discriminatory or nondiscriminatory. (*Panhandle Oil Co. v. Knox*, 277 U. S. 218, 72 L. Ed. 857; see *Indian Motorcycle Co. v. United States*, 283 U. S. 570, 75 L. Ed. 1277; *Graves v. Texas Company*, 298 U. S. 393, 80 L. Ed. 1236.) On the other hand, it is equally evident that the Supreme Court of the United States in 1937 began to whittle away the efficacy of such construction with respect to non-discriminatory taxation until finally in 1941 that Court held that the holding of the *Panhandle Oil Co.* case and its line of cases invalidating a non-discriminatory tax on federal sales was no longer tenable and upheld the validity of such a tax. (*James v. Dravo Contracting Co.*, 302 U. S. 134, 82 L. Ed. 155; *Alabama v. King & Boozer*, 314 U. S. 1, 86 L. Ed. 3; *Curry v. United States*, 314 U. S. 14, 86 L. Ed. 9; *Penn Dairies v. Milk Control Comm'n.*, 318 U. S. 261, 87 L. Ed. 748.) The effect of these decisions is that from the time of the enactment of Act 141 the meaning of the Constitution as construed by the Supreme Court of the United States underwent a complete change with respect to nondiscriminatory taxation of federal sales by a State being exempt so that after 1941 they were held to be rightful subjects of state nondiscriminatory taxation and no longer exempt therefrom under the Constitution. This later construction has not since been overruled. It is therefore controlling as well as decisive of the first basic issue provided that

what are rightful subjects of nondiscriminatory taxation for States are also ones for the Territory. Notwithstanding the sovereignty of political independence and possession of original and underived powers existing in [140] a State and the lack thereof to the Territory, there is no substantial difference between the nature and extent of a State's legislative power and those of the Territory when not curtailed by Congress, it having given full authority to the legislature of the Territory by the Organic Act in section 55 thereof to legislate upon "all rightful subjects of legislation not inconsistent with the Constitution and laws of the United States locally applicable" and having thereby vested in the legislature the full taxing power which had theretofore existed in Congress over the Territory of Hawaii. (See *Assessor v. Com. Cable Co.*, 16 Haw. 396; *Haavik v. Alaska Packers Assn.*, 363 U. S. 510, 68 L. Ed. 414; *Kitagawa v. Shipman*, 54 F. (2d) 313, aff'g. 31 Haw. 726; *Yerian v. Territory of Hawaii*, 130 F. (2d) 786, aff'g. 35 Haw. 855; *Gromer v. Standard Dredging Co.*, 224 U. S. 362, 56 L. Ed. 801.) It follows therefrom that what are rightful subjects of nondiscriminatory tax for States under the Constitution are also ones for the Territory in the absence of laws of the United States to the contrary or exempted from taxation under the Organic Act of the Territory. Whether this latter limitation exists presents the second basic issue, closely integrated to the first.

Any exemption of such rightful subjects of legislation, as are the taxpayer's gross proceeds of fed-

eral sales, from nondiscriminatory taxation by the Territory under the Organic Act would be purely objective, the test being whether the extending to them of the legislative power of the Territory is "inconsistent with the Constitution and laws of the United States locally applicable." (Organic Act § 55.) As no such inconsistency has ever existed with respect to the laws of the United States and none with respect to the Constitution after 1941, the taxpayer's gross proceeds of federal sales are not so exempt under the Organic Act. Neither being exempt under the Constitution, they therefore fall within the scope of taxation intended by the legislature and its imposition of tax upon them, [141] aside from the rate at which assessed, is a valid exercise of "the legislative power of the Territory," the specific cautionary provision of section 3 relative to their mandatory exclusion in computing the tax being inapplicable, as likewise is the general severability clause of section 24.

The taxpayer, nevertheless, contends that the legislature intended by the considered provision of section 3, *supra*, to incorporate into the Act the legal effect of the Constitution, as construed by the *Panhandle Oil Co.* case, for the purpose of limiting the Act's scope independently of any change in the meaning of the Constitution which subsequently may be attributed to it by the Supreme Court of the United States. The difficulty, however, is that the legislature expressed no such intent. The taxpayer premises his contention upon the authority of *Helvering v. Griffiths*, 318 U. S. 371, 87 L. Ed.

843, and *Parker v. Motor Boat Sales*, 314 U. S. 244, 86 L. Ed. 184. Such authority has no application to Act 141. The cases of *Helvering* and *Parker* before the Supreme Court of the United States turn upon an unequivocal legislative history of the statutes under reconsideration, the history recognizing the controlling effect of one of that Court's prior cases which had not been reversed or abrogated at the time the subject of the tax was received by the taxpayer on one hand or at the time of death of an employee on the other. In the instant case there is no such legislative history of Act 141 and at the time of its enactment the case of the Supreme Court of the United States, construing the Constitution as effecting an exemption from nondiscriminatory state taxation then in force, was no longer in force when the subjects of taxation were received and the protested tax levied. Furthermore, in the *Helvering* case the Supreme Court of the United States was urged to reverse its prior decision, which it declined to do because it could not find that Congress intended to tax the subject in question, whereas no such request was or could be made of this court, which is confronted with an existing construction of the Constitution by the Supreme Court of the United States in abrogation of its prior construction as a *fait accompli* and does find from the language of the Act itself that the legislature clearly intended to impose and authorize a tax upon the subjects in question. Again in the *Parker* case the Supreme Court of the United States refused to read a portion of the statute under consideration in a

manner that would "defeat" its purpose, whereas this court reads a portion of the Act under consideration according to the ordinary and plain meaning of its language in a manner that effectuates its purpose as well as that of the Act as a whole.

In further support of his contention, the taxpayer argues that the proviso immediately following the considered provision of section 3, *supra*, is indicative of an intention that when once an exemption from taxation under the Constitution has been construed by the Supreme Court of the United States to have existed at the time Act 141 became effective, the exception of gross proceeds of federal sales in computing the amounts of the tax imposed by the Act becomes absolute, subject to enlargement by further exemptions thereunder until such time as the Territory is permitted by Congress to tax gross proceeds derived from federal sales. To such argument I cannot accede. The pertinent part of the proviso reads: "provided, however, that if and when the Congress of the United States shall permit the Territory of Hawaii to impose a privilege tax upon gross proceeds of sales * * * derived from * * * sales made to the United States government, its departments or agencies, in * * * such event the exception(s) and exemption(s) by this section provided, shall not apply." The language of this proviso does not conflict with that of the preceding provision nor alter its meaning. Hence the broad scope of taxation intended by the legislature is unaffected thereby. Furthermore, the proviso itself has no operative force in this case in that the legislature

did not intend to make an exception of any gross proceeds of sales that are capable of being taxed by the Territory under the Constitution or Organic Act, the existence of an exemption thereunder being the condition precedent for the applicability of the exception and congressional permission the condition subsequent for the inapplicability thereof. Without more the contention of the taxpayer is untenable, he having failed to sustain his burden of establishing that his gross proceeds of federal sales come within the exception stated by the Act. (See *Re Excise Tax Rob't Hind, Ltd.*, 34 Haw. 40.)

A nondiscriminatory tax on gross proceeds of federal sales made both for use and consumption and for purposes of resale being within the Act's scope of taxation, the next question for consideration is whether the rate assessed by the tax commissioner against the taxpayer's gross proceeds or gross income derived from sales of tangible personal property, made for purposes of resale, to post exchanges and ships' services of the United States Army and Navy, respectively, is authorized by the legislature. For convenience, these sales are referred to as "post exchange sales" and post exchanges and ships' services as "post exchanges." The taxpayer in making such sales classified himself as a wholesaler and his business of selling to post exchanges as that of a wholesaler for the purpose of paying a tax assessment in respect thereto at the rate of one quarter [144] of one per cent. The commissioner reclassified the taxpayer and his business to the class and category of a retailer for the pur-

pose of assessing the rate of one and one half of one per cent. The taxpayer protests this action of the tax commissioner and challenges his authority under the Act so to do, asserting that the lower rate is the applicable one authorized by the legislature.

Recognizing that a substantial property right of the taxpayer is here involved, I neither presume that the taxpayer is attempting to avoid his duty to the Territory to pay the full amount of the tax imposed against him or that the tax commissioner is attempting to exact unjustly a greater amount of tax than authorized. I do not presuppose in favor of either, but will apply the usual test of statutory construction to declare what the legislature means by the language it has used.

The legislature in section 2, subsection 1, of the Act not only imposes privilege taxes upon "the persons on account of their business and other activities in this Territory" but also provides for the assessment and collection of those taxes. It accomplishes this by the application of percentage rates against "values, gross proceeds of sales or gross income, as the case may be" as the measure of the tax imposed. These rates are specified in paragraphs A to and including H of section 2, subsection 1, immediately following the imposition of taxation. As indicated by their running heads, these paragraphs designate the various businesses and activities with respect to which the specified rates are made applicable. The running heads are: A. Tax on manufacturers; B. Tax on retailers, wholesalers and producers; C. Tax upon contractors; D. Tax upon theaters,

amusements, radio broadcasting stations, etc.; E. Tax upon printers and publishers [145] (deleted by L. 1939, c. 252, subsec. 1); F. Tax on service business; G. Professions, and H. Tax on other business. Such are a brief of the designated businesses and activities to which rates specified by each paragraph are made applicable in measuring the tax imposed. The legislature, however, in section 4 of the Act, expressly exempts certain persons therefrom, the section having no application to the taxpayer.

The tax commissioner justifies his reclassification of the taxpayer and his selling to post exchanges to the class and category of a retailer upon section 2, subsection 1, paragraph B(1) of the Act and rests thereon his authority to assess the higher rate. This paragraph reads: "Tax on retailers, wholesalers and producers. Upon every person engaging or continuing within this Territory in the business of selling any tangible personal property whatsoever (not including, however, bonds or other evidence of indebtedness or stocks) there is likewise hereby levied and shall be assessed and collected a tax equivalent to one and one-quarter ($1\frac{1}{4}$) per cent of the gross proceeds of sales of the business; provided, however, that in the case of a wholesaler or producer the tax shall be equal to one quarter ($\frac{1}{4}$) of one per cent of the gross proceeds of sales of the business." The higher rate so specified is also specified in paragraph H of the same subsection and wherever provided in the Act has been duly increased to one and one-half ($1\frac{1}{2}$) per cent pursuant

to section 2, subsection III of the Act, as amended by Act 128 of Session Laws 1937. The percentage rate of one and one half will therefore be considered as constituting the higher rate for the purposes of this opinion.

It is evident from the Act as a whole, including the running head "Tax on retailers * * *" of paragraph B in part (1) thereof and references to "the tax on retailers" and "any person engaging or continuing in business as a retailer" of parts (2) and (3) thereof, that the "every person" referred to in part (1) of paragraph B means those "engaging and continuing within the Territory in the business of selling" as a retailer and the tax assessed accordingly at the higher rate to be the tax on retailers.

The cases of a retailer and wholesaler (that of a producer concededly having no applicability) as dealt with by the legislature are stated by the definitions of the Act. Pertinent to the case of the taxpayer, they read: "When used in this Act, unless otherwise required by the context * * * 'Retailer' shall mean any person who sells, other than as a wholesaler within the definition of this Act, tangible personal property for consumption or use by the purchaser and not for resale. * * * 'Wholesaler' * * * shall apply only to a person doing a regularly organized wholesale * * * business, known to the trade as such, and only with respect to * * * sales, to a licensed retail merchant or jobber for the purposes of resale * * *." (Section 1, (13) and (10), respectively, *supra*).

The undisputed evidence establishes that the tax-

payer in selling the tangible personal property to post exchanges was doing a regularly organized wholesale business, known to the trade as such, and that his sales were for the purposes of resale; that such sales were not for consumption or for use by the purchaser as the words "consumption" and "use" are restricted by the phrase "and not for resale" in the statutory definition of a retailer. However, such evidence also shows that the purchasing post exchanges, operating exclusively under Army Regulations [147] of the War Department, were not licensed under the Act nor required to be; that they conducted no business subject to taxation under the Act; were not wholesalers, jobbers or consumers but, as instrumentalities of the United States and arms of the War Department, they in the performance of governmental rather than proprietary functions maintained retail stores, bought for the purpose of resale and resold at the lowest possible prices to the armed forces and civilian employees of the Federal Government on army posts and naval stations for the consumption or use by such purchasers, for their convenience and for additional benefits to the armed forces not otherwise provided by the Government. (See Army Regulations No. 210-65 of the War Department; *Standard Oil Co. v. Johnson*, *supra*; *Fed. Land Bank v. Bismarck Co.*, 314 U. S. 95, 86 L. Ed. 65.)

The above facts conclusively show that the case of the taxpayer in selling tangible personal property to post exchanges did not fulfill a definitive requirement of the statutory case of a retailer in

that he clearly did not sell "for consumption or use by the purchaser and not for resale." They require, however, a consideration of whether the case of the taxpayer is that of a wholesaler within the meaning of the Act.

In determining whether the taxpayer's case is that of a wholesaler under the Act the phrase "to a licensed retail merchant or jobber" must be construed, the case of the taxpayer clearly fulfilling the other requirements relative to the nature of a wholesaler's business and the purposes of sales thereof. The alternative requirement of a "jobber" with respect to the purchaser need not be considered, post exchanges admittedly not being jobbers and the case of the taxpayer in selling to them therefore standing or falling as a case of a [148] wholesaler upon the purchasing post exchanges meeting or failing to meet the other alternative of "a licensed retail merchant." The noun "merchant" is not defined by the Act and hence its plain, ordinary and commonly accepted meaning must be taken to be the one intended. That meaning is that a merchant is "One who carries on a retail business; a storekeeper or shopkeeper." (Webster's International Dictionary, 2d ed.) This meaning is amplified by the Act's definitions of the words "retail" and "business." (§ 1, [7] and [12], respectively, *supra*.) So amplified the meaning of the noun "merchant" is one who carries on retail "activities * * * engaged in or caused to be engaged in with the object of gain or economic benefit either direct or indirect" (§ 1, [7], *supra*), in the selling of "tangible personal

property, other than by a wholesaler as such within the definition of the Act, for consumption or use by the purchaser and not for resale." (§ 1, [12], *supra*. The intended meaning of the noun "merchant" modified by the adjective "retail" is thus but a paraphrase of the noun "retailer" as defined by the Act (§ 1 [13], *supra*), and hence serves to identify the purchaser as a retailer in contradistinction to a wholesaler, jobber, or consumer. It primarily serves, however, to prevent the lower rate from being applicable to the case of a wholesaler selling to a consumer. In applying this meaning to the facts concerning the purchasing post exchanges, they admittedly not being wholesalers, jobbers or consumers, it is undisputable that they not only qualify as a "retail merchant" but meet every requirement set forth in the statutory definition of a "retailer," they carrying on retail businesses as retail storekeepers and exclusively purchasing as retailers, reselling as retailers and engaging in retail activities "with the object of * * * economic benefit either direct or indirect," if not of "gain." It is therefore evident that the only part of the requirement of a wholesaler which the case of the taxpayer in selling to them could have failed to meet is that contained in the adjective "licensed," his sales not being made to retail merchants licensed under the Act.

The employment by the legislature of the adjective "licensed" to modify a purchasing retail merchant in wholesale sales to him in my opinion is susceptible to two reasonable constructions, one being confined to the state of being licensed in a

strict statutory sense and to the implications arising from the requirements set forth in section 21 of the Act that "any person who shall have * * * gross proceeds of sales upon which a privilege tax is imposed by this Act, as a condition precedent to engaging or continuing in such business, shall * * * obtain * * *, upon payment * * * of one dollar (\$1.00), a license * * *" and the other being not so confined. In that the first readily has been adopted by the parties hereto as well as by my associates and the issues before this court having been raised under it, that construction will be considered first. Under it, the construed legislative intent would be that in order for the lower rate to be applicable the purchaser must appear to be a taxable person under the Act on subsequent retail resale, thereby preserving in a present wholesale sale the opportunity of collecting ultimately at the higher rate and where such opportunity is foreclosed by the unlicensed status of the purchaser under the Act to immediately assess the higher rate against the seller. So construed the Act would clearly not be a uniform excise tax law with respect to sales of tangible personal property sold for purposes of resale by a seller doing a regularly organized wholesale business, known to the trade as such.

The only possible explanation of why the purchasing post exchanges have an unlicensed status under the Act is because they are exempt on ultimate retail sale from taxation by the Constitution of the United States. Hence the status is merged with the constitutional exemption and is but one

of its incidents. Under the construction being considered it is evident that the constitutional exemption would not only be disregarded by it but regarded as the basic reason for the higher assessment. The legislature would be construed as attempting to obtain on immediate sale that which would be constitutionally unobtainable on subsequent resale. Such would be the effect notwithstanding the fact that the unlicensed status under the Act of purchasing post exchanges, induced by constitutional exemption, and what would be the opposing status of other purchasing retail merchants, induced by a license under the Act, have no bearing whatsoever upon their purchasing characters in immediate sales to them, but relate wholly to their respective non-taxable and taxable characters under the Act in subsequent resales, neither status affecting either the right or privilege of purchase. It would be the effect even though there is no real or substantial difference between their purchasing characters at the time of purchase, their purposes of buying being the same and the nature of their retail businesses substantially the same, and even though there is no reasonable or tenable distinction to be found in the facts that post exchanges exercised their right of purchase under authorized War Department regulations as a governmental function and other purchasing retail merchants would exercise their privilege of purchase under a license provided by the Act as a proprietary function.

“Governmental” is descriptive of the operative control of the Federal Government over post ex-

changes as its agencies in their performance of functions which, prior to their creation, [151] normally were activities of proprietary interests for the convenience of the Government's armed forces wherever stationed or operating, whereas "proprietary" is descriptive of independent ownership and the conducting of private businesses in dealing with the general public, the difference being a matter of form and not of substance. A Territory or State cannot tax post exchanges as retail merchants, not because such federal agencies perform only governmental functions as an incident of their relationship to the Federal Government, but because they are parts of a department of the Government and to tax those parts would interfere with the constitutional exercise of federal powers in which the States and their citizens as well as the Territory and its citizens are equally interested, the fundamental reason being that those powers have been delegated to the Federal Government for the common good and it may freely and constitutionally exercise them for the benefit of all. Neither can a Territory or State directly burden and impede the Government in its operation of a federal agency, engaged in a trading business normally that of proprietary interests, in a considerably larger proportion than proprietary trading businesses of the same character. In this connection a recent case of the Supreme Court of the United States forcibly brought out that "considerations bearing upon taxation by the States of activities or agencies of the federal government are not correlative with the considerations bearing upon

federal taxation of State agencies or activities." It rejected "as untenable the distinction between 'governmental' and 'proprietary' interests," stressed by its older cases, and upheld the validity of a nondiscriminatory federal tax upon a State engaged in the business of bottling mineral water, even [152] though such business is conceived by the State to be for the public benefit and "has relation to its conservation policy." (*New York et al. v. United States*, 90 L. Ed. 265, 268, 270, decided Jan. 14, 1946. See *South Carolina v. United States*, 199 U. S. 437, 50 L. ed. 261; *Helvering v. Powers*, 293 U. S. 214, 79 L. ed. 291; *Allen v. Regents*, 304 U. S. 439, 82 L. ed. 1448.)

There being no real or substantial difference between the actual character as purchasers of post exchanges and other retail merchants, licensed under the Act, nor a reasonable or tenable distinction between the nature of their retail business and the purposes and functions of buying at the time of purchase, it follows that there is none between sales to them when made for purposes of resale as was by the taxpayer while doing a regularly organized wholesale business known to the trade as such, the character of the seller, that of the merchandise sold and that of the subjects taxed being the same. Nor is such state of equality disturbed by the apparent equal treatment under the Act with respect to sales for purposes of resale to constitutionally exempt purchasers and those exempted by the Act itself, post exchanges and other retail merchants, licensed under the Act, constituting a class beyond and with-

out the classifications of those exempted by the Act. The legislature may, with the approval of Congress, exempt any otherwise taxable person and has the power to withdraw the exemption granted either in whole or in part at any time within its discretion as dictated by the equitable and economic necessities of the case. Presumably pursuant thereto, the legislature by enacting Act 141 has with one hand in effect extended exemptions to certain otherwise taxable persons as well as to public utilities of the Territory and its subdivisions and with the other hand partly withheld [153] the full force of such exemptions from such persons as well as impliedly consenting thereto with respect to such public utilities. However, it cannot withdraw nor effectively consent to that which it did not give. Neither can it take away any part of an immunity impliedly granted under the Constitution. The considerations with respect to persons exempted by the Act thus have no relation to those exempted under the Constitution and the fact that the Act would happen to operate equally with respect to sales to them is immaterial. It is only with respect to the unequal operation of the Act, as construed, towards substantially the same purchasers, who are not exempted by the Act and constitute no part of the Territory, that this court should be concerned. The question, therefore, is whether, as contended by the taxpayer, the assessment of the higher rate with respect to sales to post exchanges which are constitutionally exempt on resale, when the lower rate is assessed with respect to sales to such other retail merchants

not so exempt, would constitute a discriminatory tax that directly trespasses upon the immunity impliedly afforded by the Constitution to post exchanges and renders the legislative authority to assess at the higher rate unconstitutional and invalid.

In considering this question the practical operation and effect of the Act under the considered construction at the time of purchase must be determined. It is obvious that the Act would operate to tax gross proceeds of sales to post exchanges at a rate six times greater than that which would be assessed against those to other retail merchants and by so doing would impose upon post exchanges in the exercise of their right of purchase a relatively greater burden than that upon the others in the exercise of their privilege of purchase. In addition, [154] it would place an excessive burden upon the right of purchase of post exchanges that would not be imposed had they not been clothed with an implied constitutional immunity. It likewise is obvious that the effect thereof directly would tend to discourage sales to post exchanges while encouraging those to other retail merchants. Such treatment unquestionably would be unfair and injurious to post exchanges. It would be so marked, in my opinion, as to transcend that which is merely impolitic or improvident. It justifies the inference that the Act as construed would be unfriendly in design, favoring forms of proprietary retail businesses within the Territory which are in competition to government retail businesses. Therefore it is clear to

me that such an ununiform excise tax law would be discriminatory in so far as the exercise of the right of purchase by post exchanges is concerned. This, however, would not be a matter of legislative intent to single out post exchanges nor dependent upon a hostile attitude by the legislature towards them but the result of the construed legislative intent to realize the highest amount of revenue possible under the Act, which is ordinarily the motive behind discriminatory legislation, and the actual operation in affecting a method for making the higher percentage rate applicable in lieu of the lower.

Discrimination is synonymous with an unreasonable distinction. It is the antithesis of fairness. It means, in this case, the unfair placing of an excess of burden upon the right of purchase of post exchanges not placed upon the corresponding privilege of purchase of other retail merchants and which would not be placed with respect to post exchanges had they not been constitutionally exempted from the correlative tax at the higher rate on resale. The Act thus would treat more harshly a right [155] which the Territory did not give than a privilege extended by it. Had the purchasing post exchanges not been so exempt, the only rate that would be assessable against them under the Act would be the higher percentage rate. In that case, the Act would operate uniformly and nondiscriminately towards them and other retail merchants. However, such is not the case. Post exchanges are so exempt and under the considered construction the Act without

uniformity would operate discriminately towards them in favor of the others, operating in disregard of constitutional immunity of post exchanges and making such immunity the basis of its discriminatory assessment on sales to them. The attendant unfairness and favoritism thereof on immediate sales to such purchasers would not be cured by the effect of the Act's unequal operation upon their divergent states of taxability on subsequent resales by them nor is it an answer to say that the two inequalities would give an overall tax burden to the other purchasing retail merchants that would be greater by a relative one-quarter per cent than that of post exchanges. The obvious answer is that such a burden upon the other retail merchants should be proportionately greater by a relative one and one-half per cent if the constitutional exemption of post exchanges from that rate is to be justly respected. However, it is not for this court to indulge in mathematical speculations or attempt to balance differences in the overall ultimate burdens of purchasers who are substantially the same, but it should confine itself to the question at hand respecting the particular and immediate sales under consideration where there undeniably would be a marked excess of burden inflicted upon the right of purchase of post exchanges not imposed upon the comparable privilege of other retail merchants nor would be inflicted had [156] the purchasing post exchanges not been constitutionally exempt. There in lies the discriminatory character of the assessment in this case, there being at the time of purchase no real or sub-

stantial difference nor reasonable or tenable distinction between the actual purchasing character, retail business, purpose and function of buying of post exchanges and those of the other retail merchants.

As stated by Mr. Justice Frankfurter in rendering the opinion of the Court in *New York et al. v. United States*, supra, at page 271 of volume 90 of the Law Edition of United States Reports: “* * * ‘discrimination’ is not a code of specific but a continuous process of application” and as pointed out by Mr. Justice Holmes in his dissenting opinion in the *Panhandle Oil Co.* case (the dissent being later in effect sustained) at page 223 of volume 277 of United States Reports, “* * * this Court which so often has defeated the attempt to tax in certain ways can defeat an attempt to discriminate or otherwise go too far without wholly abolishing the power to tax. The power to tax is not the power to destroy while this Court sits. The power to fix rates is the power to destroy if unlimited, but this Court while it endeavors to prevent confiscation does not prevent the fixing of rates.” Thus, discrimination being a continuous process of application, it follows that if the Territory has the power to fix a discriminatory rate with respect to sales to post exchanges substantially higher than with those to other retail merchants it could fix one still higher and so could the States, thereby effectively expelling post exchanges from territorial and state limits, drying up at its source the necessary flow of merchandise and rendering post exchanges unable to function in defeat of the purpose for which they were created.

It is evident therefrom that the power to fix [157] a discriminatory rate is unlimited and hence the power which destroys. This court, in my opinion, should therefore defeat such an attempt to discriminate and prevent the confiscatory assessments from being applied, the pertinent issue under the considered construction being whether the assessment made by the tax commissioner would trespass upon the implied constitutional immunity of post exchanges as an immediate or direct interference with the Government's constitutional powers to operate them under the Constitution. (Const., Art. I, § 8.)

The pith of the majority decision of the *Panhandle Oil Co.* case is that any state tax on sales to a federal agency, regardless of the character and degree of interference of that tax with government, is unconstitutional and invalid because it infringes upon the implied constitutional immunity of that purchasing agency to have the constitutional independence of the United States remain untrammelled in respect to such purchases, the stated reasons being that "It is immaterial that the seller and not the purchaser is required to report and make payment to the State. Sale and purchase constitute a transaction by which the tax is measured and on which the burden rests" and "The necessary operation of these enactments when so construed is directly to retard, impede and burden the exertion by the United States of its constitutional powers" to operate such agency. (*Panhandle Oil Co. v. Knox*, 277 U. S. 218, 222.) What proved to be the case's point of vulnerability, however, is that it went too far and in-

validated a nondiscriminatory tax. In his dissent thereto, Mr. Justice Holmes pointed to the ground upon which the cases of *James v. Dravo Contracting Co.*, *Alabama v. King & Boozer*, *Curry v. United States* and *Penn Dairies v. Milk Control Commission*, all *supra*, subsequently overruled its broad holding. This ground he stated at page 225 of volume 277, *supra*, [158] in the closing sentence of his dissent as follows: "The question of interference with Government, I repeat, is one of unreasonableness and degree and it seems to me that the interference in this case [i. e., that of a nondiscriminatory tax] is too remote." The bracketed explanation is supplied by me not only by reason of an analysis of the enactments considered in the *Panhandle Oil Co.* case but from the only authority cited by Mr. Justice Holmes in support of the stated ground of dissent. This authority is the case of *Metcalf & Eddy v. Mitchell*, 269 U. S. 514, wherein the Supreme Court declared on pages 524 and 525 thereof that "The tax is imposed without discrimination upon income whether derived from services rendered to the State or services rendered to private individuals. In such a situation it cannot be said that the tax is imposed upon an agency of government in any technical sense, and the tax itself cannot be deemed to be an interference with Government, or an impairment of the efficiency of its agencies in any substantial way." The reasoning for such a ground is found in the following language of Mr. Justice Holmes' dissent at page 224 of volume 277, *supra*: "To come down more closely to

the question before us, when the Government comes into a State to purchase I do not perceive why it should be entitled to stand differently from any other purchaser. It avails itself of the machinery furnished by the State and I do not see why it should not contribute in the same proportion that every other purchaser contributes for the privileges that it uses."

The Dravo case in holding that a nondiscriminatory state tax upon gross receipts from a contract with the Federal Government is not unconstitutional as a paid tax on the contract itself or as otherwise directly burdening the Government [159] rested its decision squarely upon the authority of the Metcalf & Eddy case, at pages 156 and 157 of volume 302 of United States Reports, and thus adopted the ground upon which Mr. Justice Holmes dissented. Likewise the King & Boozer case, in deciding that the view prevailing in the Panhandle Oil Co. case and its line of cases that a nondiscriminatory tax on sales to a federal agency is unconstitutional has ceased to be tenable, cited as the leading case that of Metcalf & Eddy and relied on the Dravo case. Also the Curry case, companion to that of King & Boozer, rested its decision on the King & Boozer case. Furthermore the Penn Dairies case at page 269 of volume 318 of United States Reports, in deciding that "the mere fact that nondiscriminatory taxation of the contractor imposes an increased economic burden on the Government is no longer regarded as bringing the contractor within any implied immunity of the Gov-

ernment from state taxation or regulation," relied upon the *Metcalf & Eddy*, *Dravo* and *King & Boozer* cases. Thus the pivotal point of these cases in overruling the one of *Panhandle Oil Co.* is the nondiscriminatory character of the taxes upheld by them. They lay down the general rule that there is no implied constitutional immunity of the Government and its agencies from nondiscriminatory state taxation upon persons dealing with them, the converse thereof by necessary implication being that there is such an immunity from discriminatory state taxation.

By making no distinction whatsoever in the character of the state tax enactments considered and none in the degree of interference with government, it stands to reason that the majority opinion of the *Panhandle Oil Co.* case (which condemned as unconstitutional an operation of statute that was in fact [160] equally disposed to purchasing federal agencies and all other purchasers and passed upon them a fair economic burden, incidental and normal, involving but a remote interference with government) necessarily included within its condemnation an unfair and injurious operation to purchasing federal agencies that passes to them an excessive economic burden not borne by other competitive purchasers and would not be borne by the federal agencies had they not been exempt under the Constitution, which is proximate and abnormal involving a direct and destructive interference with government. The significance of such inclusion is brought into bold relief by the overruling of that

majority opinion, which in effect removed nondiscriminatory state taxes from the otherwise authoritative holding of the *Panhandle Oil Co.* case. It is evident that it was overruled only with respect to such taxes and their lower degree of interference with government, the overruling thereby being limited to that character of taxes and degree and not affecting the majority opinion with respect to discriminatory taxes and their higher degree of interference with government. It is apparent, therefore, that the reasoning of the majority opinion in the *Panhandle Oil Company* case, advanced by the court to establish a direct interference with government, is unimpaired when applied to a discriminatory tax and hence controls the question presented, decisive of the pertinent issue, that discriminatory tax directly impedes, retards and burdens the constitutional exercise of the powers of the Government to maintain its agencies. Thus the *Panhandle Oil Co.* case, construed in the light of the implied converse of the rule, subsequently laid down by the Supreme Court, as well as in the light of the consideration of fair dealing and equality which have been the philosophy of this nation since its inception, is an authority for the rule of law that a discriminatory tax by State or Territory [161] upon sales to a federal agency is unconstitutional and invalid as a direct infringement upon the constitutional exercise of the powers of the United States to operate such an agency. This authority is squarely in point. There is no need, therefore, to go further by way of analogy and draw a parallel of corresponding effect from the

wealth of authorities pertaining to the unconstitutionality of including other forms of implied constitutional immunity within the measure of a tax (see *Missouri v. Gehner*, 281 U. S. 313, 74 L. ed. 870; *Nat'l. Life Ins. Co. v. United States*, 277 U. S. 508, 72 L. ed. 968; *Miller v. Milwaukee*, 272 U. S. 713, 71 L. ed. 487; *Northwestern Ins. Co. v. Wisconsin*, 275 U. S. 136, 72 L. ed. 203; *Macallen Co. v. Massachusetts*, 279 U. S. 620, 73 L. ed. 874), or to the unconstitutional discrimination, violative of the guarantee of "equal protection of the laws" under the Fourteenth Amendment of the Constitution, of making the character of the taxpayer exercising a privilege the basis for a higher tax than that upon competitive others under similar circumstances exercising the same privilege. (See *Southern Railway Co. v. Greene*, 216 U. S. 400, 54 L. ed. 536; *Bethlehem Motors Co. v. Flynt*, 256 U. S. 421, 65 L. ed. 1029; *Quaker City Cab Co. v. Penna.*, 277 U. S. 389, 72 L. ed. 927; *Concordia Fire Ins. Co. v. Illinois*, 292 U. S. 535, 78 L. ed. 1141.)

For the reasons assigned herein the discriminatory assessment at the higher rate with respect to the case of the taxpayer in selling to post exchanges is the direct result of the statutory construction considered. It renders, in my opinion, the assessment thereof unconstitutional and invalid. I cannot perceive, however, that the legislature intended to enact a void provision, it being presumed to intend that which is constitutional and valid. To my mind the legislature intended to [162] enact a uniform excise tax law without discrimination.

The employment by the legislature of the adjective "licensed" in modifying the purchasing "retail merchant" in order to make applicable the lower rate to the case of a wholesaler is susceptible to a more reasonable and less narrow construction and which is not confined wholly to the strict statutory sense of the adjective in securing a license under the Act. It is that the purchaser must be a retail merchant who is lawfully permitted by proper authority to carry on a retail business within the Territory which without such permission would be illegal. In this connection it is significant that the Act defines neither the adjective "licensed" nor the noun "license." Hence the plain, ordinary and accepted meaning of the adjectives must be taken as the one intended. This meaning is that a licensed purchaser is one who has "Authority or liberty given to do or forbear any act; permission to do something (specified); esp., a formal permission from the proper authorities to perform certain acts or to carry on a certain business which without such permission would be illegal; also, the document embodying such permission * * *." (Webster's International Dictionary, 2d ed.) Applying it to the facts concerning post exchanges, it is very evident that they come completely within it. They have the permission in the form of Army Regulations of the War Department, pursuant to congressional enactments (16 Stat. 315, 319; 18 Stat. 337), to carry on retail businesses within the Territory from the United States as the proper authority under the Constitution, the authorized War Department reg-

ulations being the document embodying such permission and having the force of law. Post exchanges are therefore duly licensed retail merchants. Any contention of difference between [163] them and the other retail merchants would be purely fanciful, nor can it be reasonably argued that the legislature ever intended to classify wholesale sales made to retail merchants, duly licensed within the Territory by the War Department in accordance with federal law under the Constitution, differently from those made to retail merchants duly licensed by the tax commissioner in accordance with territorial law under the Act, both purchasers being retailers who are equally law abiding.

Construing the adjective "licensed" in conformity with its plain, ordinary and accepted meaning, the Act is a uniform excise tax law with respect to wholesale sales and operates without discrimination in making applicable the lower rate to the case of a wholesaler. It does so equitably with respect to wholesale sales made to all licensed retail merchants within the Territory, regardless of the source of the purchasers' permission to carry on retail businesses therein so long as it is derived from a proper authority and without such permission the conduct thereof would be illegal. Thus construed the Act does not infringe upon or disregard the implied constitutional immunity of purchasing post exchanges engaged in the retail business in the exercise of their right to buy at wholesale within the Territory for purposes of resale. The resultant economic burden passed to them is a remote and fair one as a normal incident of the tax which rests in the same

proportion upon all purchasers similarly engaged and exercising comparable rights or privileges who are not exempted by the Act and constitute no part of the Territory, the validity of the tax so assessed at the lower rate not being dependent upon that burden's ultimate resting place. It is well settled that such a nondiscriminatory assessment of a uniform excise tax is constitutional and valid. (*James v. Dravo Contracting Co.*, [164] *Alabama v. King & Boozer*, *Curry v. United States*, *Penn. Daries v. Milk Control Comm'n.*, all *supra*; *Western L. Co. v. State Board of Equalization*, 11 Calif. [2d] 156, 78 P. [2d] 731; *Federal Land Bank v. DeRochford*, 69 N. D. 382, 297 N. W. 522; *Compress of Union v. Stone*, 188 Miss. 49, 193 So. 329.) In my opinion this reasonable construction reflects the true legislative intent of the Act, consonant with its constitutionality and validity, and should be adopted.

I concur in the result of the majority opinion with respect to the tax upon the taxpayer's gross proceeds of sales, made for use and consumption, to the United States but dissent therefrom for the reasons stated with respect to the other tax upon his sales, made for purposes of resale, to post exchanges.

In my opinion the cause should be remanded below with instructions to set aside the judgments and enter ones in favor of the taxpayer for recovery of the excess of the tax paid over the assessment at the rate of one quarter of one per cent against his gross proceeds of post exchange sales.

/s/ LOUIS LE BARON.

[Endorsed]: Filed March 4, 1946. [165]

In the Supreme Court of the Territory of Hawaii

No. 2581

THOMAS H. BRODHEAD,

Plaintiff, Defendant-in-Error,

vs.

WILLIAM BORTHWICK, Tax Commissioner of
the Territory of Hawaii,

Defendant, Plaintiff-in-Error.

No. 2583

THOMAS H. BRODHEAD, d.b.a. T. H. BROD-
HEAD CO.,

Plaintiff, Defendant-in-Error,

vs.

WILLIAM BORTHWICK, Tax Commissioner of
the Territory of Hawaii,

Defendant, Plaintiff-in-Error.

Action To Recover Gross Income
Taxes Paid Under Protest

Error To Circuit Court, First Judicial Circuit,
Honorable J. A. Matthewman, Fifth Judge,
Presiding

PETITION FOR REHEARING

Comes now the above-named Plaintiffs, Defendants-in-Error, Thomas H. Brodhead and Thomas H. Brodhead, d.b.a. T. H. Brodhead Co., being

aggrieved by the decision of this Honorable Court, filed March 5, 1946, reversing the judgments of the court below and remanding these causes for a new trial, and presents his petition for a rehearing of the above-entitled causes, and, in support thereof, respectfully shows: [167]

I.

That although urged to do so by counsel for Plaintiffs, Defendants-in-Error, this Court has omitted from consideration in its opinion filed in the above-entitled causes on March 4, 1946, the proposition that the Territory of Hawaii cannot lawfully impose a tax on sales to post exchanges and ships' service stores at a higher rate with respect to such sales than with respect to sales to other retail merchants as an indirect way of doing what cannot be done directly under the Constitution of the United States.

The Opinion of the Court by a statement of its conclusions (on page 1 thereof) affirms the proposition that a tax, the legal effect of which is to lay a direct and immediate tax upon the instrumentalities of the United States, is within the implied prohibition of the Constitution of the United States against laying a burden upon or interfering with federal activities even though imposed under the guise of an excise tax. It is submitted that the Territorial excise tax under consideration is a direct and immediate tax upon an instrumentality of the United

States within the foregoing proposition by reason of the administrative application of the taxing act and not merely by reason of the fact that in its incidence it might indirectly reach a federal instrumentality. As specially pointed out by the dissenting Associate Justice in his opinion (on page 22 thereof) the majority decision of the *Panhandle Oil Co.* case stands as good authority for its statements that "It is immaterial that the seller and not the purchaser is required to report and make payment to the State. Sale and purchase constitute a transaction by which the tax is measured and on which the burden rests" and "the necessary operation of these enactments [168] when so construed is directly to retard, impede and burden the exertion by the United States of its constitutional powers" to operate such agency. (*Panhandle Oil Co. vs. Knox*, 277 U. S. 218, 222). In other words, the tax involved in these cases is a direct tax on the sale and purchase in the transfer of goods from the taxpayer to post exchanges and ships' service stores. As the legislature could not lawfully impose such a direct tax at a higher rate on sales to post exchanges and ships' service stores than to other retail merchants, it is urged that administrative authority cannot so apply the taxing act. In the cases under consideration, the administrative application of the taxing act makes it a direct tax on post exchanges and ships' service stores which discriminates by charging a higher rate on sales to post exchanges and ships' service stores than to other retail merchants merely because they are instrumentalities

of the United States. In fact, it defeats the very reason post exchanges and ships' service stores are operated as instrumentalities of the United States: that of providing a means of supplying articles of necessity and convenience which the government cannot supply, at the lowest possible prices to our citizen Army and Navy personnel, the great majority of whom have been forced to serve their country for very low pay.

This matter is respectfully pointed out without intent to argue with the Court's opinion, but to focus the Court's attention on its failure to consider the argument and the cases cited beginning on page 45 of the Answering Brief of Plaintiff, Defendant-in-Error, heretofore filed herein, that the tax involved is a direct tax resulting from administrative application which attempts to do by indirection [169] that which could not be done directly.

II.

That in viewing Act 141, Session Laws of Hawaii 1935, as a classification to taxpayers by the legislature and an assessment of a different rate of taxation to each class this Court has failed to consider whether this classification is a "proper classification" not resulting in discrimination.

This Court has found that the legislature in enacting Section 2, B, of Act 141, Session of Law of Hawaii 1935, has classified taxpayers. For example,

“wholesalers,” as defined by the Act, is a class separate from and carved out of “every person” as a class, the one being taxed at the rate of one-quarter of one per cent and the other at the rate of one and one-half per cent. The Court has also reiterated the well-settled rules that the legislature has the power to classify for the purposes of taxation and that diversity of rate of taxation based upon “proper classification” is not discrimination. But the majority of the Court has not considered or stated whether the particular application of the tax involved in these cases resulted in a “proper classification,” which is a classification without discrimination, as has the dissenting Associate Justice in his exhaustive and carefully reasoned dissent on this point.

The majority of the Court has refused in its reasoning on juridicial discrimination to take the next logical step and recognize that the practical effect of the classification as seen by the Court is to place this taxpayer in a class made up of “every person” who sells to [170] instrumentalities of the United States, which obviously discriminates against the United States. The taxpayer has been held to be “not a ‘wholesaler’ as defined by the Act;” he is certainly not within the definition of a “retailer” or a “producer” as set forth in the Act; he does not, in the instances under consideration, sell to one specifically exempted by the Act under a grant of an exemption by the Legislature which may at any time be withdrawn by the Legislature. The

taxpayer is then in the only class conceivably left—"every person" who sells to the Federal government.

In finding that factually no discrimination exists against post exchanges and ships' service stores (Opinion of the Court, page 10) the Court has not taken into consideration that which was pointed out in the dissenting opinion that discrimination is not a code of specifics but a continuous process of application. The practical effect of the application of the tax involved to sales to post exchanges and ships' service stores is illustrated when viewed in the light of the times. Although it may not be specifically stated in the record the Court may take notice of this period as one of scarcity of consumer merchandise. Consider what happens when both licensed retailers and post exchanges and ships' service stores are attempting to secure the same merchandise from the taxpayer's warehouses. The taxpayer pays tax, on the one hand, at the rate of one-quarter of one per cent when he sells that merchandise to a retail merchant licensed under the act, and he pays, on the other hand, at the rate of one and one-half per cent (or six times the first rate) when he sells to post exchanges and ships' service stores under the administration of the act by the Territory. To whom is it more profitable for him to sell? Certainly it is obvious that the application of a tax, the practical effect of which is to keep merchandise away from post exchanges and ships' service stores because they are instrumentali-

ties of the United States, render the tax discriminatory in its application. It is respectfully urged that the Court consider this point on a rehearing.

III.

That instead of rendering a final judgment based upon its decision, this Court has acted under a misapprehension of the record in remanding the cause for a new trial, there being nothing apparent in the record to be gained by either party in a new trial.

In this connection, the Court's attention is directed to the record of the trial of these cases in the court below and the Assignments of Errors accompanying the Applications for Writ of Error in each case. The record shows no controversy existed concerning the facts of these cases. It is actually revealed by the record that these cases were submitted to the court below almost entirely on stipulated facts. Recognition of this status of the facts is found in the Assignments of Errors in these cases in that no error is assigned to the trial of the cases but all errors are specifically directed to the judgment of the court below and the decision upon which such judgment was rendered.

Under Section 9564, Revised Laws of Hawaii 1945, this Court may

“... affirm, reverse or modify the order, judgment or sentence of the trial court. It [172] may enter such order, judgment or sentence, or may remand the case to the trial court for

entry of the same or for such other or further proceedings, as in its opinion the facts and law warrant. It may correct any error appearing on the record . . .”

In these cases, where the opinion of the Court may be readily applied to the stipulated facts, it is respectfully submitted that the entry of a final judgment by this Court more properly follows the usual procedure of applying this Court's decision upon Writs of Error.

Wherefore, Plaintiffs, Defendants-in-Error, respectfully pray that this petition for a rehearing be granted, and that the judgment of the Court below be, upon further consideration, affirmed, and that final judgment to that effect be entered by this Honorable Court.

Dated: Honolulu, T. H., March 22, 1946.

THOMAS H. BRODHEAD and
THOMAS H. BRODHEAD d.b.a.
T. H. Brodhead Co., Plaintiffs,
Defendants-in-Error,

By SMITH, WILD, BEEBE &
CADES,

By /s/ MILTON CADES,
Their Attorneys.

CERTIFICATE OF COUNSEL

I, Milton Cades, counsel for the above named Plaintiffs, Defendants-in-Error, do hereby certify

that the foregoing petition for a rehearing of these causes is presented in good faith and not for delay.

/s/ MILTON CADES.

[Endorsed]: Filed March 22, 1946. [173]

In the Supreme Court of the Territory of Hawaii

October Term, 1945

Thomas H. Brodhead v. William Borthwick,
Tax Commissioner of the Territory of Hawaii

Nos. 2581 and 2583

DECISION
ON PETITION FOR REHEARING

Filed March 22, 1946. Decided March 27, 1946.

Kemp, C.J.; Peters and Le Baron, J.J.

Per Curiam. This is a petition for rehearing. The opinion in the case to which the motion refers is reported ante on page 314.

Grounds of the motion are as follows:

(1) That the court "omitted from consideration in its opinion * * * the proposition that the Territory of Hawaii cannot lawfully impose a tax on sales to post exchanges and ships' service stores at a higher rate with respect to such sales than with respect to sales to other retail merchants as an indirect way of doing what cannot be done directly under the Constitution of the United States";

(2) That in viewing Act 141, Session Laws of

Hawaii 1935, as a classification of taxpayers by the legislature and an assessment of a different rate of taxation to each class, this court has failed to consider whether this classification is a "proper classification" not resulting in discrimination;

(3) That instead of rendering a final judgment [175] based upon its decision, this court has acted under a misapprehension of the record in remanding the cause for a new trial, there being nothing apparent in the record to be gained by either party in a new trial.

The grounds of the motion will be considered seriatim.

(1) As we interpreted the brief of the taxpayer, repeated upon oral argument, he contended that no tax liability existed but that if there did the applicable rate was one-quarter of one per cent and that the application by the taxing authorities of the higher rate of one and one-half per cent was inconsistent with the plain terms of the Act, unlawful and discriminatory. If under the law the imposition of the higher rate was mandatory and as thus construed was applied by the taxing authorities in assessing the tax, discrimination, if any, was the result of the Act itself and not of any unlawful action on the part of the administrative offices enforcing the Act. We held that the taxpayer was liable to a tax under the Act and that the rate of one-quarter of one per cent applicable to a "wholesaler" did not apply. We further held that under the terms of the Act the rate of one and one-

half per cent applicable to "every person" did apply and that the assessment by the taxing authorities was consistent with the terms of the Act. As a result the objection of discrimination had relation only to the terms of the Act itself and not to the acts of the administrative offices enforcing the Act. If the rate applied was not discriminatory under the law, obviously the law as administered was not discriminatory. The subject of discrimination therefore [176] was treated accordingly and fully discussed. The opinion itself is sufficient refutation of the charge.

(2) This ground seeks to reargue the subject of discrimination upon which the court was divided. The dissent adopted the thesis of the taxpayer; the majority held differently. The composite represents the considered effort of both parties and reargument would serve no useful purpose. A dissent does not rate a rehearing.

(3) Although the better practice seems to be to move to amend the remand, this ground will nevertheless be considered.

The within action is one at law.¹ It was tried jury waived. And is subject to all the provisions of law applicable to actions at law, jury waived, including the requirement that "the court shall hear and decide the cause, both as to the facts and the law, and its decision shall be rendered in writing stating its reasons therefor."² The powers of this

¹R. L. H. 1945, § 9647.

²R. L. H. 1945, § 10107.

court upon error to review a judgment in an action at law, jury waived, is purely appellate. It does not include the power to decide the facts.

No error was reserved or assigned requiring or admitting the summary entry of judgment in this court. The power reposed in this court by Revised Laws of Hawaii 1945, section 9564, to enter judgment, as in its opinion the facts and law warrant, should not be invoked by this [177] court of its own motion while the statutory duties of the trial court in respect thereto remain incomplete.

The petition for rehearing is denied without argument.

By the Court:

[Seal] /s/ LEOTI V. KRONE,
 Clerk.

SMITH, WILD, BEEBE &
CADES,
For the Petition.

Approved:

 /s/ S. B. KEMP,
 Chief Justice.

 /s/ E. C. PETERS,
 Associate Justice.

.....
 Associate Justice.

[Endorsed]: Filed March 27, 1946. [178]

In the Supreme Court of the Territory of Hawaii

No. 2631

THOMAS H. BRODHEAD, d.b.a. T. H. BROD-
HEAD CO.,

Plaintiff-Appellant,

vs.

WILLIAM BORTHWICK, Tax Commissioner of
the Territory of Hawaii.

Defendant-Appellee.

Action to Recover Gross Income Taxes
Paid Under Protest

Error To Circuit Court, First Judicial Circuit
Honorable A. M. Christy, Second Judge, Presiding

PETITION FOR APPEAL

To the Honorable Chief Justice and Associate Jus-
tices of the Supreme Court of the Territory of
Hawaii:

Comes now, Thomas E. Brodhead, doing business
as T. H. Brodhead Co., Plaintiff-Appellant above-
named, by his attorneys, Smith, Wild, Beebe &
Cades, deeming himself aggrieved by the judgment
of the above-entitled Court in the above-entitled
cause, which judgment was made and entered on
February 25, 1947, and claiming that there are
manifest and material errors to the damage of said
Thomas H. Brodhead, doing business as T. H. Brod-
head Co., in said cause, which errors are spe-
cifically set forth in the Assignment of Errors filed

herewith, to which reference is hereby made, and respectfully prays that an appeal may be allowed in the above-entitled cause and that he be allowed to prosecute said appeal to the United States Circuit Court of Appeals for the Ninth Circuit, in accordance with the statutes in such cases made and provided; and that the Clerk of the Supreme Court of the Territory of Hawaii be directed to send the United States Circuit Court of Appeals for the Ninth Circuit a transcript of the record, proceedings and papers in [180] this cause, duly authenticated, for the correction of the errors complained of, and that a citation may issue.

And in this behalf, said Thomas H. Brodhead, doing business as T. H. Brodhead Co., shows that said judgment was rendered on Writ of Error from the judgment of the Circuit Court, First Judicial Circuit, Territory of Hawaii, in the above-entitled Court and cause, and involves the Constitution and the laws of the United States of America, and that the value in controversy, exclusive of interest and costs, exceeds Five Thousand Dollars (\$5,000.00).

Dated: Honolulu, T. H., May 22, 1947.

SMITH, WILD, BEEBE &
CADES,

By MILTON CADES,
Attorneys for Thomas H. Brodhead, doing business
as T. H. Brodhead Co.

Territory of Hawaii,
City and County of Honolulu—ss.

Milton Cades, being first duly sworn, on oath deposes and says: That he is a partner of the firm of Smith, Wild, Beebe & Cades, attorneys for the Plaintiff-Appellant named in the foregoing Petition for Appeal; that he has read the foregoing Petition for Appeal, and that the matters and things therein set forth are true of his own knowledge, and that the value in controversy, exclusive of interest and costs, exceeds \$5,000.00.

MILTON CADES.

Subscribed and sworn to before me this 22nd day of May, 1947.

FRIEDA H. ROBERT,

Notary Public, First Judicial Circuit, Territory of
Hawaii.

My commission expires 6-30-49.

Service of a copy of the foregoing Petition for Appeal is hereby admitted this 22nd day of May, 1947.

/s/ C. NILS TAVARES,

Attorney General, Territory of Hawaii, Attorney
for the Tax Commissioner.

I do hereby certify that the foregoing is a full, true and correct copy of the original on file in the

office of the Clerk of the Supreme Court of the Territory of Hawaii.

Dated at Honolulu, T. H., May 22, 1947.

[Seal]

GUS SPROAT,

Clerk, Supreme Court, Territory of Hawaii.

[Title of Supreme Court and Cause.]

ASSIGNMENT OF ERRORS

Comes now the above-named Thomas H. Brodhead, doing business as T. H. Brodhead Co., and files the following assignment of errors upon which it will rely in the prosecution of the appeal herewith petitioned for in the said cause to the United States Circuit Court of Appeals for the Ninth Circuit from the judgment of this Court entered on the 25th day of February, 1947:

(1) The Supreme Court erred in affirming the judgment of the Circuit Court, First Judicial Circuit, Territory of Hawaii, that the Plaintiff-Appellant take nothing by his complaint and dismissing the action, and in failing to set aside the judgment of said Circuit Court.

(2) The Supreme Court erred in holding that the General Excise Tax Law of the Territory of Hawaii (Act 141, Ser. A-44, Sess. Laws of Hawaii 1935, as amended), herein referred to as the "Excise Tax Law," imposes a tax, and for the period from October 1, 1942, through March 31, 1944, did

impose a tax upon the Plaintiff-Appellant with respect to sales of tangible personal property made to the United States Government, its departments and agencies.

(3) The Supreme Court erred in holding that Section 3 of said law did not exempt the plaintiff from tax on the gross proceeds of sales made by him to the United States Government and its post exchanges and Ship's Service Stores.

(4) The Supreme Court erred in failing to hold that the Legislature in enacting said Excise Tax Law intended to exempt from taxation the proceeds of sales to the United States, its departments and agencies.

(5) The Supreme Court erred in holding that the tax as so imposed does not levy a burden upon or interfere with Federal activities.

(6) The Supreme Court erred in failing to hold that said Excise Tax Law so administered as to include the gross receipts from sales to the United States, its agencies or instrumentalities, within the measure of tax, is a tax on the United States which is within the prohibition of the rule against the taxation of a sovereign.

(7) The Supreme Court erred in failing to hold that the tax as so imposed is a direct burden on the Federal Government in the exercise of its essential governmental power of raising and supporting armies and of providing and maintaining a Navy, and that said tax therefore violates Article I, Sec-

tion 8, Clauses 12 and 13, of the Constitution of the United States.

(8) The Supreme Court erred in holding that such tax had only an economic effect upon the United States Government, its departments and agencies, which economic effect is indirect and does not constitute the tax an invalid burden upon or interference with Federal activities. [184]

(9) The Supreme Court erred in holding that the imposition of said tax was and is within the power of the Legislature of the Territory under Section 55 of the Hawaiian Organic Act and not in violation of Article I, Section 8, Clause 12 or 13, or the Fifth Amendment of the Constitution of the United States.

(10) The Supreme Court erred in failing to hold that said tax violates the Fifth Amendment of the Constitution of the United States in that it constitutes a tax on the privilege of doing business with the United States, its agencies or instrumentalities.

(11) The Supreme Court erred in failing to hold that said tax did not violate Section 55 of the Hawaiian Organic Act in that it imposes a direct tax on the privilege of doing business with the United States which is a subject beyond the legislative power of the Legislature of the Territory of Hawaii, in that it is not a rightful subject of legislation and in that it is inconsistent with the Constitution and laws of the United States.

(12) The Supreme Court erred in holding that

the rate of tax imposed by said General Excise Tax Law upon all gross proceeds of sales to the Federal Government and agencies thereof was at the rate of $11\frac{1}{2}\%$ irrespective of whether such goods were intended to be or were resold by the purchasers.

(13) The Supreme Court erred in holding that the tax imposed by said law upon the gross proceeds of sales to United States Post Exchanges and Ship's Service Stores for the purpose of resale was at a rate higher than $\frac{1}{4}$ of 1%.

(14) The Supreme Court erred in holding that a tax on sales to Post Exchanges and Ship's Service Stores at a higher rate than on sales to other retailers is not prohibited as an indirect [185] way of doing what cannot be done directly under the Constitution of the United States.

(15) The Supreme Court erred in holding that said tax law required the Tax Commissioner to include in the measure of tax the proceeds of sales to the United States and its agencies at the rate of $11\frac{1}{2}\%$.

(16) The Supreme Court erred in holding that the administrative practice, whereby the rate of tax on sales to Post Exchanges and Ship's Service Stores was increased because of a judicial determination that Post Exchanges and Ship's Service Stores could not be constitutionally taxed on their sales, did not show that the purpose of the administrators was to accomplish an unlawful result by an indirect method.

(17) The Supreme Court erred in holding that the classifications made by the Legislature are “natural and reasonable and not discriminatory” against the plaintiff or the Federal Government or its instrumentalities.

(18) The Supreme Court erred in holding that Post Exchanges and Ship’s Service Stores are not “merchants” within the meaning of the tax law.

(19) The Supreme Court erred in holding that a tax upon plaintiff at a higher rate on account of its sales to Ship’s Service Stores and Post Exchanges for resale than upon its sales to licensed retailers for resale was not discriminatory against the plaintiff or the Federal Government or its instrumentalities.

(20) The Supreme Court erred in holding that the Tax Commissioner did not discriminate in the administration of the tax law against the plaintiff or the Federal Government or its instrumentalities.

(21) The Supreme Court erred in holding in the Decision and Judgment made and entered in this cause that the plaintiff is not entitled to recover the gross income taxes paid by him under protest or any part thereof for the reason that the Legislature specifically exempted such gross proceeds of sales from the tax law; for the further reason that the Legislature is without power to impose a tax upon the proceeds of gross sales to the United States or its instrumentalities; and for the further reason that in no event can the Legislature impose a tax

upon the gross proceeds of sales to Ship's Service Stores and Post Exchanges for resale at a higher rate than that imposed on account of sales to other retailers for resale, namely $\frac{1}{4}$ of 1%.

(22) The Supreme Court erred in failing to make a judgment in favor of the plaintiff that he recover gross income taxes paid under protest in accordance with his prayer as set forth in the complaint.

Wherefore, Thomas H. Brodhead, doing business as T. H. Brodhead Co., prays that the said judgment of the Supreme Court of the Territory of Hawaii may be reversed, and for such other and further relief as to the Court may seem just and proper.

Dated: Honolulu, T. H., this 22nd day of May, 1947.

SMITH, WILD, BEEBE &
CADES,

By MILTON CADES,
Attorneys for Plaintiff-Appel-
lant.

Service of a copy of the foregoing Assignment of Errors is hereby admitted this 22nd day of May, 1947.

/s/ C. NILS TAVARES,
Attorney General, Territory of Hawaii, Attorney
for the Tax Commissioner.

I do hereby certify that the foregoing is a full,

true and correct copy of the original on file in the office of the clerk of the Supreme Court of the Territory of Hawaii.

Dated at Honolulu, T. H., May 22, A.D. 1947.

[Seal] GUS K. SPROAT,
Clerk, Supreme Court, Terri-
tory of Hawaii.

[Title of Supreme Court and Cause.]

ORDER ALLOWING APPEAL AND FIXING
AMOUNT OF BOND

Upon reading and filing the verified Petition for Appeal presented to this Court by Thomas H. Brodhead, doing business as T. H. Brodhead Co., in which he prays that an appeal may be allowed him to the United States Circuit Court of Appeals for the Ninth Circuit from the judgment of this Court made and entered in the above entitled Court and cause on February 25, 1947, wherein it is alleged that manifest and material errors have occurred, to the end that said errors, if any there be, may be speedily corrected and justice done in the premises; and upon said Thomas H. Brodhead, doing business as T. H. Brodhead Co., filing an Assignment of Errors, together with said Petition for Appeal, and together with a bond for costs in the sum of Two Hundred Fifty Dollars (\$250.00);

It Is Hereby Ordered that said appeal to the United States Circuit Court of Appeals for the

Ninth Circuit be and the same is hereby allowed, and that said bond for costs in the amount of Two Hundred Fifty Dollars (\$250.00), filed by said Thomas H. [189] Brodhead, be and it is hereby approved.

Dated: Honolulu, T. H., May 22, 1947.

[Seal] /s/ S. B. KEMP,

Chief Justice of the Supreme Court of the Territory of Hawaii.

Attest:

[Seal] LEOTI V. KRONE,
Clerk.

Service of a copy of the foregoing Order Allowing Appeal and Fixing Amount of Bond is hereby admitted this 22nd day of May, 1947.

/s/ C. NILS TAVARES,

Attorney General, Territory of Hawaii, Attorney for William Borthwick, Tax Commissioner.

I do hereby certify that the foregoing is a full true and correct copy of the original on file in the office of the clerk of the Supreme Court of the Territory of Hawaii.

Dated at Honolulu, T. H., May 22, 1947.

/s/ LEOTI V. KRONE,
Clerk, Supreme Court,
Territory of Hawaii. [190]

[Endorsed]: Filed May 22, 1947.

[Title of Supreme Court and Cause.]

BOND ON APPEAL

Know All Men By These Presents:

That Thomas H. Brodhead, as principal and Pacific Insurance Co., Ltd., a Hawaiian corporation, as surety, are held and firmly bound unto William Borthwick, Tax Commissioner of the Territory of Hawaii, Defendant-Appellee, in the sum of \$250.00 for the payment of which well and truly to be made, said Thomas H. Brodhead, as principal and Pacific Insurance Co., Ltd., as surety, do bind themselves, their respective heirs, executors, administrators, successors and assigns, jointly and severally, and firmly by these presents.

The Condition of This Obligation Is Such That:

Whereas the above bounden principal, Thomas H. Brodhead, doing business as T. H. Brodhead Co., has filed its Petition for an Appeal to the United States Circuit Court of Appeals for the Ninth Circuit from the judgment entered in the above-entitled cause by the Supreme Court of the Territory of Hawaii; [192]

Now, Therefore, if the said principal shall prosecute said appeal with effect and answer all costs if he fails to sustain said appeal, then this obligation shall be void, otherwise it shall remain in full force and effect.

In Witness Whereof, said Thomas H. Brodhead has hereunto set his hand, and said Pacific Insurance Co., Ltd., has caused its name to be signed and

the corporate seal affixed by its proper officers thereunto duly authorized this 21st day of May, 1947.

/s/ THOMAS H. BRODHEAD,
Principal,

PACIFIC INSURANCE CO.,
LTD.,

By /s/ GEO. H. McDONOUGH,
Its Treasurer.

[Seal] By
Its Surety.

The foregoing bond is hereby approved as to form, amount and sufficiency of surety.

/s/ SAMUEL B. KEMP,

Chief Justice of the Supreme Court of the Territory of Hawaii.

Service of a copy of the foregoing Bond on Appeal is hereby admitted this 22nd day of May, 1947.

/s/ C. NILS TAVARES,

Attorney General, Territory of Hawaii, Attorney for William Borthwick, Tax Commissioner.

I do hereby certify that the foregoing is a full true and correct copy of the original on file in the office of the clerk of the Supreme Court of the Territory of Hawaii.

Dated May 22, 1947.

/s/ LEOTI V. KRONE,
Clerk, Supreme Court,
Territory of Hawaii.

[Endorsed]: Filed May 22, 1947.

[Title of Supreme Court and Cause.]

2

CITATION ON APPEAL

The United States of America—ss.

The President of the United States of America to
William Borthwick, Tax Commissioner and Tax
Collector of the Territory of Hawaii, and to the
Attorney General of the Territory of Hawaii,
his Attorney, Greeting:

You, and each of you, are hereby cited and admonished to be and appear before the United States Circuit Court of Appeals for the Ninth Circuit, in the City of San Francisco, State of California, within forty (40) days from the date of this citation, pursuant to an appeal duly allowed and filed in the Office of the Clerk of the Supreme Court of the Territory of Hawaii on May 22, 1947, in said cause, wherein Thomas H. Brodhead, doing business as T. H. Brodhead Co., is appellant, and you are appellee, to show cause, if any there be, why the judgment made and entered in the Supreme Court of the Territory of Hawaii on February 25, 1947, should not be corrected and speedy justice done to the parties in [195] that behalf.

Witness the Honorable Fred M. Vinson, Chief Justice of the United States of America, this 22nd day of May, 1947.

[Seal] /s/ SAMUEL B. KEMP

Chief Justice of the Supreme Court of the Territory
of Hawaii.

Attest:

[Seal] LEOTI V. KRONE
Clerk.

Service of the foregoing Citation of Appeal is
hereby admitted this 22nd day of May, 1947.

/s/ C. NILS TAVARES

Attorney General, Territory of Hawaii, Attorney
for William Borthwick, Tax Commissioner.

I do hereby certify that the foregoing is a full,
true and correct copy of the original on file in the
office of the clerk of the Supreme Court of the Ter-
ritory of Hawaii.

Dated May 22, 1947.

/s/ LEOTI V. KRONE,
Clerk, Supreme Court,
Territory of Hawaii.

[Endorsed]: Filed May 22, 1947.

[Title of Supreme Court and Cause.]

AMENDED PRAECIPE

To Leoti V. Krone, Clerk of the Supreme Court of
the Territory of Hawaii:

You will please prepare a transcript of the record
in the above entitled cause, to be filed in the office

of the Clerk of the United States Circuit Court of Appeals for the Ninth Circuit, and include in said transcript the following, which are on file in said cause, to wit:

- (1) Complaint, Exhibit "A" and Summons.
- (2) Answer.
- (3) Stipulation dated June 24, 1944, and Exhibits "B" to "D," inclusive.
- (4) Decision of Honorable A. M. Cristy, Judge, Circuit Court, First Judicial Circuit, filed May 15, 1946.
- (5) Judgment of Circuit Court filed May 15, 1946.
- (6) Reporter's' transcript of proceedings.
- (7) Reporter's transcript of proceedings in the Matter of Thomas H. Brodhead vs. William Borthwick, Law No. 16,956, Circuit Court of the First Judicial Circuit, Pages 1 to 30.
- (8) All Exhibits in Law No. 16,956.
- (9) Writ of Error filed in Supreme Court, Territory of Hawaii.
- (10) Assignment of Errors to the judgment of the Circuit Court.
- (11) Stipulation re submission without oral argument, filed February 24, 1947.
- (12) Decision of Supreme Court, filed February 25, 1947.
- (13) Judgment of Supreme Court, filed February 25, 1947.

- (14) Opinion of Supreme Court in Nos. 2581 and 2583, together with Petition for Rehearing and Decision thereon.
- (15) Petition for Appeal.
- (16) Assignment of Errors.
- (17) Order Allowing Appeal and Fixing Amount of Bond.
- (18) Bond on Appeal.
- (19) Citation on Appeal.
- (20) All orders enlarging time to docket cause in the Ninth Circuit Court of Appeals.
- (21) This Amended Praecipe.

Dated: Honolulu, T. H., this 26th day of June, 1947.

SMITH, WILD, BEEBE & CADES

By /s/ MILTON CADES

Attorneys for Plaintiff-Appellant.

Service of a copy of the foregoing Amended Praecipe is hereby admitted this 28th day of June, 1947, and consent is hereby given to the amendment of the Praecipe originally filed in the form above set forth.

/s/ RHODA V. LEWIS

Assistant Attorney General, Territory of Hawaii,
Attorney for Tax Commissioner.

I do hereby certify that the foregoing is a full, true and correct copy of the original on file in the

office of the clerk of the Supreme Court of the Territory of Hawaii.

Dated June 27, 1947.

/s/ LEOTI V. KRONE,
Clerk, Supreme Court,
Territory of Hawaii.

[Endorsed]: Filed June 27, 1947.

[Title of Supreme Court and Cause.]

ORDER EXTENDING TIME TO AUG. 15, 1947

Good cause appearing therefor,

It Is Hereby Ordered that plaintiff-appellant herein may have to and including August 15, 1947, within which to file his record on appeal in the United States Circuit Court of Appeals for the Ninth Circuit.

Dated: Honolulu, T. H., June 27, 1947.

[Seal] /s/ SAMUEL B. KEMP
Chief Justice, Supreme Court,
Territory of Hawaii.

[Endorsed]: Filed June 27, 1947.

[Title of Supreme Court and Cause.]

CLERK'S CERTIFICATE TO CERTIFIED
RECORD ON APPEAL

I, Leoti V. Krone, clerk of the supreme court of

the Territory of Hawaii, do hereby certify that the foregoing documents, attached hereto, and listed in the index herein, are full, true, and correct copies of certified copies and of originals on file in the above-entitled court and cause.

I further certify that the cost of the foregoing transcript of record on appeal to the United States Circuit Court of Appeals for the Ninth Circuit is \$202.74, and that said amount has been paid by the attorneys for appellant.

In Witness Whereof, I have hereunto set my hand and affixed the seal of the supreme court of the Territory of Hawaii at Honolulu, this 11th day of July, 1947.

[Seal] /s/ LEOTI V. KRONE
Clerk.

[Endorsed]: No. 11688. United States Circuit Court of Appeals for the Ninth Circuit. Thomas H. Brodhead, doing business as T. H. Brodhead Co., Appellant, vs. William Borthwick, Tax Commissioner and Tax Collector of the Territory of Hawaii, Appellee. Transcript of Record. Upon Appeal from the Supreme Court for the Territory of Hawaii.

Filed July 14, 1947.

/s/ PAUL P. O'BRIEN,
Clerk of the United States Circuit Court of Appeals
for the Ninth Circuit.

In the United States Circuit Court of Appeals
for the Ninth Circuit

No. 11688

THOMAS H. BRODHEAD, doing business as

T. H. Brodhead Co.,

Appellant,

vs.

WILLIAM BORTHWICK, Tax Commissioner of
the Territory of Hawaii,

Appellee.

STATEMENT OF POINTS AND
DESIGNATION OF PARTS OF RECORD

Comes now Thomas H. Brodhead, doing business as T. H. Brodhead Co., Appellant herein, by and through his attorneys, Urban E. Wild and Milton Cades, and in compliance with Subdivision 6 of Rule 19 requiring a concise statement of the points on which Appellant intends to rely on the appeal, hereby adopts as the points on appeal the Assignment of Errors appearing in the transcript of the record, and, in compliance with the rules of this Court pertaining to the designation of the portion of the record to be printed, directs that the entire Record on Appeal, as set forth in the Amended Praecipe heretofore filed with the Clerk of the Supreme Court of the Territory of Hawaii with the request that copies of the record as so designated

be prepared and transmitted to this Court, be printed as the record on review.

Dated at Honolulu, T. H., July 14th, 1947.

/s/ URBAN E. WILD,

/s/ MILTON CADES,

Attorneys for Appellant.

Of Counsel:

SMITH, WILD, BEEBE & CADES,
Fourth Floor, Bishop Trust Building,
Honolulu, T. H.

Service of a copy of the foregoing Statement of Points and Designation of Parts of Record is hereby admitted this 14th day of July, 1947.

/s/ RHODA V. LEWIS,

Acting Attorney General, Territory of Hawaii,
Attorney for Tax Commissioner.

[Endorsed]: Filed July 17, 1947.

No. 11,688

IN THE
United States Circuit Court of Appeals
For the Ninth Circuit

THOMAS H. BRODHEAD, doing business
as T. H. Brodhead Co.,

Appellant,

vs.

WILLIAM BORTHWICK, Tax Commis-
sioner and Tax Collector of the Ter-
ritory of Hawaii,

Appellee.

Upon Appeal from the Supreme Court for the
Territory of Hawaii.

BRIEF FOR APPELLANT.

URBAN E. WILD,

MILTON CADES,

Bishop Trust Building, Honolulu, T. H.,

Attorneys for Appellant.

SMITH, WILD, BEEBE & CADES,

Bishop Trust Building, Honolulu, T. H.,

Of Counsel.

FILE

DEC 9 - 1947

PAUL P. O'BRIEN,

CLERK



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No. 11,688

IN THE
United States Circuit Court of Appeals
For the Ninth Circuit

THOMAS H. BRODHEAD, doing business
as T. H. Brodhead Co.,

Appellant,

vs.

WILLIAM BORTHWICK, Tax Commis-
sioner and Tax Collector of the Ter-
ritory of Hawaii,

Appellee.

Upon Appeal from the Supreme Court for the
Territory of Hawaii.

BRIEF FOR APPELLANT.

STATEMENT AS TO JURISDICTION.

This case involves the tax liability of appellant under Act 141 (Series A-44), Session Laws of Hawaii 1935, as amended, hereinafter referred to as the "General Excise Tax Law", and arises from an action brought in the Circuit Court, First Judicial Circuit, Territory of Hawaii, pursuant to Section 571, Revised Laws of Hawaii 1935, to recover taxes paid under protest (R. 2). Judgment was entered on September 13, 1944, for the recovery by appellant of the money paid under protest. A writ of error issued out of the

Supreme Court of the Territory of Hawaii on September 16, 1944. By order of the court, this case (No. 2583), and a similar case (No. 2581), were consolidated for briefing and hearing.

In an opinion covering the consolidated cases filed on March 4, 1946, the Supreme Court, with one justice dissenting, reversed the judgment appealed from and remanded the case for a new trial (R. 191). The petition for a rehearing of the appellant, filed March 22, 1946 (R. 238), was denied on March 27, 1946 (R. 246), and an order reversing the judgment appealed from and remanding the cause for a new trial was filed on April 9, 1946. On May 15, 1946, judgment dismissing the action was filed in the Circuit Court, First Judicial Circuit, Territory of Hawaii (R. 107), and, on August 7, 1946, a writ of error issued out of the Supreme Court (R. 177). On February 25, 1947, the Supreme Court, with one justice dissenting, affirmed the judgment of the Circuit Court (R. 187), and entered judgment accordingly (R. 189). On May 22, 1947, this appeal was filed pursuant to Sec. 128 of the Judicial Code (28 U.S.C.A., Sec. 225) (R. 259).

This case involves the Constitution of the United States, particularly Article I, Section 8, Clauses 12 and 13, and the Fifth Amendment thereto. It also involves statutes of the United States, particularly the Organic Act of the Territory of Hawaii (April 30, 1900, 31 Statutes at Large 141, Chapter 339, as amended).

The value in controversy, exclusive of interest and costs, exceeds \$5000.00.

STATEMENT OF THE CASE.

Appellant, Thomas H. Brodhead, a resident of Honolulu, City and County of Honolulu, Territory of Hawaii, during the period here in question, was the general partner of a registered special partnership doing business under the firm name and style of T. H. Brodhead Co. (R. 19-20).

Appellee is, and was at all relevant times, the duly appointed, qualified and acting Tax Commissioner of the Territory of Hawaii, and as such, is and was in charge of the administration of the General Excise Tax Law (R. 20).

Appellant, during the period here in question, carried on a regularly established wholesale business, known to the trade as such (R. 148-149). Appellant filed gross income tax returns, in all respects as required by the General Excise Tax Law, for the period in question (R. 20).

From the time of enactment of the General Excise Tax Law in 1935 until after December 31, 1941, no taxes under the General Excise Tax Law were attempted to be imposed by the Territory of Hawaii with respect to sales to the United States, its agencies or instrumentalities (R. 152-3, 155), except with respect to the proceeds of construction contracts as distinguished from sales and purchase contracts (R. 156). Sales to post exchanges were sought to be taxed at $\frac{1}{4}$ of 1% during this time under an Attorney General's opinion to the effect that post exchanges were not agencies or instrumentalities of the United States (R. 155-6). Commencing on

January 1, 1942, the Territory attempted to impose a tax upon sales to the United States (R. 156). A notice of the change in administrative practice was advertised for ten days, beginning December 31, 1941, the notice stating that such sales had previously been "exempt" (R. 167-168). At the same time, the Territory purported to increase the tax on sales to post exchanges from $\frac{1}{4}$ of 1% to 1½% (R. 156-7). The rate was stated by the Territory to have been increased at that time because it had been determined that post exchanges were instrumentalities of the United States although no evidence was adduced showing a basis for this change (R. 160, 162-3).

On May 2, 1944, appellee issued "First Notices of Proposed Additional Assessment of Gross Income Tax" for the indicated periods, increasing the tax of appellant as follows:

October 1 to December 31, 1942

<u>Business Activity</u>	<u>Additional Amt. Taxable</u>	<u>Rate</u>	<u>Additional Tax</u>	
Retail Sales				
Post Exchanges	\$ 49,602.24	1½%	\$ 744.03	
Retail Sales				
Ships' Service Stores	81,383.69	1½%	1,220.76	
Retail Sales				
Other Federal Sales	2,120.40	1½%	31.81	\$ 1,996.60

January 1 to December 31, 1943

Retail Sales				
Post Exchanges	\$155,266.67	1½%	\$2,329.00	
Retail Sales				
Ships' Service Stores	291,044.42	1½%	4,365.67	
Retail Sales				
Other Federal Sales	440.67	1½%	6.61	\$ 6,701.28

January 1 to March 31, 1944

Retail Sales				
Post Exchanges	\$ 33,444.20	1½%	\$ 501.66	
Retail Sales				
Ships' Service Stores	81,036.44	1½%	1,215.55	
Retail Sales				
Other Federal Sales	723.99	1½%	10.86	\$ 1,728.07
Total Tax.....				<u><u>\$10,425.95</u></u>

(R. 21.)

All of said sales were reported by appellant on his returns, but the income therefrom was claimed as exempt as derived from sales to the United States and its post exchanges and ships' service stores.¹ Moreover, appellant, on his returns, classified the

¹Wherever "post exchanges" is used herein, it is meant to include ships' service stores in accordance with the stipulation of the parties hereto (R. 25).

sales to post exchanges as wholesale sales, taxable (if subject to tax) at the rate of $\frac{1}{4}$ of 1%. Appellee disallowed the claimed exemption. In addition, appellee disallowed the wholesale classification of sales to post exchanges, and reclassified the same as retail sales, taxable at the rate of $1\frac{1}{2}\%$ (R. 22).

On May 15, 1944, appellant paid, under protest, the sum of \$10,425.95 so assessed (R. 22); the chief grounds of protest set forth being as follows:

1. That gross income derived from said sales to the United States and its post exchanges is not taxable under the provisions of the General Excise Tax Law;

2. That if taxable under said law, such tax is in violation of the Organic Act of the Territory of Hawaii and the Constitution of the United States;

3. If the proceeds of sales to post exchanges can lawfully be taxed, the rate thereon cannot exceed $\frac{1}{4}$ of 1% (R. 12-14).

The trial court held that under Section 3 of the General Excise Tax Law the Legislature did not intend to impose a tax upon gross proceeds of, or gross income from federal sales, and rendered judgment accordingly for full recovery of the tax paid (R. 205). On appeal, the Territorial Supreme Court held that the Legislature did intend to tax such sales and construed the statute as one imposing a tax on the gross proceeds of sales to the United States and its agencies and instrumentalities. Further, it held that the Legislature had power to impose such a tax, and that the taxation on account of sales to post exchanges at

a higher rate than on account of sales to other retailers for resale does not constitute discrimination. Accordingly, it reversed the judgment of the trial court and remanded the case for a new trial (R. 191). Upon retrial, the cause was submitted on the record of the prior trial, and the court found for defendant in accordance with the decision of the Territorial Supreme Court (R. 107). Upon appeal to the Territorial Supreme Court by appellant, that court affirmed the judgment below (R. 189). From that judgment this appeal is taken (R. 259).

QUESTIONS OF LAW INVOLVED.

1. Can the Territory of Hawaii lawfully impose a tax on the gross proceeds of sales to the United States, its agencies or instrumentalities?

2. Assuming, without admitting, that the answer to the first question is in the affirmative, can the Territory of Hawaii lawfully impose a tax on the wholesaler at a higher rate on the gross receipts from sales to post exchanges for resale than on the gross receipts from sales by the same wholesaler to other retail merchants for resale?

STATUTES INVOLVED.

The applicable provisions of said General Excise Tax Law (Act 141 [Ser. A-44] Session Laws of Hawaii 1935), as amended, are as follows:

“Section 1. *Definitions.* When used in this Act, unless otherwise required by the context:

* * * * *

(10) 'Wholesaler' or 'jobber' shall apply only to a person doing a regularly organized wholesale or jobbing business, known to the trade as such, and only with respect to the following sales: (a) sales, to a licensed retail merchant or jobber, for purposes of resale;

* * *

'Wholesaler' or 'jobber' shall mean a person, or a definitely organized division thereof definitely organized to render and rendering a general distribution service which buys and maintains at his or its place of business a stock or lines of merchandise which he or it distributes; and which, through salesmen, advertising or sales promotion devices, sells to licensed retailers, or to institutional, or licensed commercial or industrial users, in wholesale quantities and at wholesale rates.

* * * * *

(12) 'Retail' means the sale of tangible personal property, other than by a wholesaler as such within the definition of this Act, for consumption or use by the purchaser and not for resale.

(13) 'Retailer' shall mean any person who sells, other than as a wholesaler within the definition of this Act, tangible personal property for consumption or use by the purchaser and not for resale.

* * * * *

Section 2. *Imposition of tax; rates.*² 1. There

²Commencing July 1, 1939 all 1¼% rates were raised to 1½% by order of the Governor (see subsection III relating to increase or decrease of rates; by Act 111 S.L. 1947, effective July 1, 1947, the 1½% rate was raised to 2½%, and the ¼% rate was raised to 1%).

is hereby levied and shall be assessed and collected annually privilege taxes against the persons on account of their business and other activities in this Territory measured by the application of rates against values, gross proceeds of sales or gross income, as the case may be as follows:

* * * * *

B. Tax on retailers, wholesalers and producers. (1) Upon every person engaging or continuing within this Territory in the business of selling any tangible personal property whatsoever (not including, however, bonds or other evidence of indebtedness or stocks) there is likewise hereby levied, and shall be assessed and collected, a tax equivalent to one and one-quarter ($1\frac{1}{4}$) per cent of the gross proceeds of sales of the business; provided, however, that in the case of a wholesaler or producer, the tax shall be equal to one-quarter ($\frac{1}{4}$) of one per cent of the gross proceeds of sales of the business.

(2) Provided, that gross proceeds of sales of tangible property in interstate and foreign commerce shall constitute a part of the measure of the tax imposed on retailers and wholesalers, to the extent, under the conditions and in accordance with the provisions of the Constitution of the United States and the Acts of the Congress of the United States which may be now in force or may be hereafter adopted.

* * * * *

H. Tax on other business. Upon every person engaging or continuing within this Territory in any business, trade, activity, occupation, or calling not included in the preceding subsections or any other provisions of this Act, there

is likewise hereby levied and shall be assessed and collected, a tax equal to one and one-quarter ($1\frac{1}{4}$) per cent of the gross income thereof. This subsection shall apply to the gross income of persons taxable under other subsections hereof not derived from the exercise of privileges taxable thereunder.

* * * * *

Section 3. *Interstate and foreign commerce.* *Federal agencies.* In computing the amounts of any tax imposed under this Act, there shall be excepted from the gross proceeds of sales or gross income, so much thereof as is derived from sales of tangible property in interstate and foreign commerce, which under the Constitution of the United States, the Territory of Hawaii is, or may hereafter be, prohibited from taxing, or is derived from any sales made to the United States government, its departments or agencies, which is, or may hereafter be, exempted from taxation under the Constitution of the United States or the Organic Act of the Territory; provided, however, that if and when the Congress of the United States shall permit the Territory of Hawaii to impose a privilege tax upon gross proceeds of sales or gross income derived from sales of tangible personal property in interstate and foreign commerce, or from sales made to the United States government, its departments or agencies, in either such event the exceptions and exemptions by this section provided, shall not apply.

* * * * *

Section 21. *Licenses; penalty for failure to secure.* Any person who shall have a gross income or gross proceeds of sales upon which a privilege tax is imposed by this Act, as a condition

precedent to engaging or continuing in such business, shall in writing apply for and obtain from the tax commissioner, upon payment of the sum of one dollar (\$1.00) a license to engage in and to conduct such business for the current tax year, upon condition that he shall pay the taxes accruing to the Territory under the provisions of this Act, and he shall thereby be duly licensed to engage in and conduct such business. Said license shall be renewed annually and shall expire on the thirty-first day of December next succeeding the date of its issuance. Licenses and applications therefor shall be in such form as the commissioner shall prescribe, except that where the licensee is engaged in two or more forms of business of different classification, the license shall so state on its face. Any person who may lawfully be required by the Territory, and who is required by this Act, to secure a license as a condition precedent to engaging or continuing in any business subject to taxation under this Act, who shall engage or continue in such business without securing such license in conformity with this Act, shall be guilty of a misdemeanor; and any director, president, secretary or treasurer of a corporation who permits, aids or abets such corporation to engage or continue in business without securing a license in conformity with this Act, shall likewise be guilty of a misdemeanor; the penalty for such misdemeanor shall be that prescribed by section 19 for individuals, corporations or officers of corporations, as the case may be, for violation of said section 19."

SPECIFICATION OF ERRORS RELIED ON.

The Supreme Court of the Territory of Hawaii erred:

(1) In affirming the judgment of the Circuit Court, First Judicial Circuit, Territory of Hawaii, that the appellant take nothing by his complaint and dismissing the action, and in failing to set aside the judgment of said Circuit Court.

(2) In holding that the General Excise Tax Law imposing a tax on the gross proceeds of sales of appellant to the United States Government and its post exchanges, does not levy a burden upon or interfere with federal activities.

(3) In failing to hold that the General Excise Tax Law, including the gross receipts from sales to the United States, its agencies or instrumentalities, within the measure of tax, is a tax on the United States which is within the prohibition of the rule against the taxation of the sovereign.

(4) In failing to hold that the tax as so imposed is a direct burden on the Federal Government in the exercise of its essential governmental power of raising and supporting armies and of providing and maintaining a navy, and that said tax, therefore, violates Article I, Section 8, Clauses 12 and 13, of the Constitution of the United States.

(5) In holding that such tax had only an economic effect upon the United States Government, its departments and agencies, which economic effect is indirect and does not constitute the tax an invalid burden upon or interference with federal activities.

(6) In holding that the imposition of said tax was and is within the power of the Legislature of the Territory of Hawaii under Section 55 of the Hawaiian Organic Act and in violation of Article I, Section 8, Clause 12 or 13, of the Fifth Amendment of the Constitution of the United States.

(7) In failing to hold that said tax violates the Fifth Amendment of the Constitution of the United States in that it constitutes a tax on the privilege of doing business with the United States, its agencies or instrumentalities.

(8) In holding that said tax does not violate Section 55 of the Hawaiian Organic Act in that it imposes a direct tax on the privilege of doing business with the United States, which is a subject beyond the legislative power of the Territory of Hawaii in that it is not a rightful subject of legislation and in that it is inconsistent with the Constitution and laws of the United States.

(9) In holding that the rate of tax imposed by said General Excise Tax Law upon all gross proceeds of sales to the Federal Government and agencies thereof was at the rate of 11½% irre-

spective of whether such goods were intended to be or were resold by the purchasers.

(10) In holding that the tax imposed by said law upon the gross proceeds of sales to post exchanges for the purpose of resale was at a rate higher than $\frac{1}{4}$ of 1%.

(11) In holding that said tax law required the Tax Commissioner to include in the measure of tax the proceeds of sales to the United States and its agencies at the rate of $1\frac{1}{2}\%$.

(12) In holding that a tax on sales to post exchanges at a higher rate than on sales to other retailers is not prohibited as an indirect way of doing what cannot be done directly under the Constitution of the United States.

(13) In holding that the classifications made by the Legislature between post exchanges and licensed retailers are natural and reasonable and not discriminatory against appellant or the Federal Government or its instrumentalities.

(14) In holding that a tax upon appellant at a higher rate on account of its sales to post exchanges for resale than upon its sales to licensed retailers for resale was not discriminatory against appellant or the Federal Government or its instrumentalities.

(15) In holding that the Tax Commissioner did not discriminate in the administration of the tax law against appellant or the Federal Government or its instrumentalities.

(16) In holding that appellant is not entitled to recover the gross income taxes paid by him under protest, or any part thereof, for the reason that the Legislature is without power to impose a tax upon the proceeds of gross sales to the United States or its instrumentalities, and, for the further reason that in no event can the Legislature impose a tax upon the gross proceeds of sales to post exchanges for resale at a higher rate than that imposed on account of sales to other retailers for resale.

(17) In failing to enter a judgment in favor of appellant that he recover gross income taxes paid under protest in accordance with his prayer as set forth in the complaint.

SUMMARY OF ARGUMENT.

A—The Territory of Hawaii cannot lawfully impose a tax on the gross receipts from sales to the United States or its agencies or instrumentalities.

1. The Territory of Hawaii is not a sovereign government with inherent power to impose taxes, but derives its power to tax from the United States.
2. Congress has never delegated to the Territory of Hawaii the power to tax the United States or its agencies or instrumentalities.
3. A statute which includes the gross receipts from sales to the United States or its agencies

or instrumentalities, within the measure of the tax, is a tax on the United States.

4. The Panhandle line of cases has not been overruled in so far as it holds that a tax on account of sales to the United States is unconstitutional.

B—The Territory of Hawaii cannot lawfully impose a tax at a higher rate with respect to sales to post exchanges than with respect to sales to other retail merchants for resale.

1. The General Excise Tax Law properly construed does not impose a tax at a higher rate with respect to sales to post exchanges than with respect to sales to other retailers.
2. Assuming that the General Excise Tax Law requires the imposition of a higher rate with respect to sales to post exchanges than with respect to sales to other merchants, then said Act is unconstitutional.

ARGUMENT.

A. THE TERRITORY OF HAWAII CANNOT LAWFULLY IMPOSE A TAX ON THE GROSS RECEIPTS FROM SALES TO THE UNITED STATES OR ITS AGENCIES OR INSTRUMENTALITIES.

1. The Territory of Hawaii is not a sovereign government with inherent power to impose taxes, but derives its power to tax from the United States.

The right of the Territory to tax the gross receipts from sales to the United States and to its agencies and instrumentalities is upheld by the Supreme Court of

the Territory by analogy to comparatively recent cases, which, it is claimed, support the right of states to impose such taxes.

No taxes were attempted to be imposed by the Territory with regard to sales to the United States, its agencies, or instrumentalities until after December 31, 1941. However, assessments were made with respect to the proceeds of construction contracts with the United States. Sales to post exchanges were sought to be taxed at the rate of $\frac{1}{4}$ of 1% during such time.³ It was stated by the Deputy Tax Commissioner in charge of gross income taxes to have been done under the theory that post exchanges were not agencies or instrumentalities of the United States. The exemption of sales to the United States, prior to January 1, 1942, arose out of the fact that since the enactment of the General Excise Tax Law in 1935, and until the end of 1941, the proper officers, charged with the duty of administering taxes in the Territory, by and with the advice of the legal officers of the Territory, recognized that the Territory was without constitutional power to impose a tax with regard to such sales. At that time it was generally recognized throughout the country in all the courts, including the Supreme Court of the United States, that under the holdings in *Graves v. Texas Co.*,⁴ *Panhandle Oil Co. v. Mississippi ex rel. Knox*,⁵ and *Indian Motorcycle Co. v.*

³The legality of such tax appears not to have been judicially determined.

⁴298 U.S. 393, 80 L. ed. 1236 (1936).

⁵277 U.S. 218, 72 L. ed. 857 (1928).

United States,⁶ states were without power to impose taxes on the gross receipts from sales to the United States or its agencies or instrumentalities. The generality of the holdings in these cases has been somewhat limited by later decisions of the United States Supreme Court.⁷ However, the direct holding of the Supreme Court that no tax can be imposed by a state upon the gross receipts from sales to the United States or its agencies or instrumentalities is still preserved. It is our contention that the court below proceeds on a false assumption when it argues, by analogy from cases involving states' right to tax, that the Territory has a similar right to tax gross receipts from sales to the United States and its agencies and instrumentalities.

In the first place, the Supreme Court has not held that states may tax with regard to sales to the United States and its agencies and instrumentalities. The cases relied on and cited by the court do not so hold. In *James v. Dravo Contracting Co.*, *supra*, the Supreme Court said that the *Panhandle* case, *supra*, and *Graves v. Texas Co.*, *supra*, can be distinguished and must be held limited to their facts; and, in *Alabama v. King & Boozer*, *supra*, the Supreme Court founded its holding on the fact that the purchaser was not the United States or its agency or instrumentality.⁸

⁶283 U.S. 570, 75 L. ed. 1277 (1931). These cases are hereinafter sometimes referred to as the *Panhandle* line of cases.

⁷*James v. Dravo Contracting Co.*, 302 U.S. 134, 82 L. ed. 155 (1937); *Alabama v. King & Boozer*, 314 U.S. 1, 86 L. ed. 3 (1941); *Curry v. United States*, 314 U.S. 14, 86 L. ed. 9 (1941).

⁸These cases are discussed more fully *infra*.

In the second place, the Territorial Supreme Court loses sight of the inherent difference in the fundamental nature of states and territories. By the Constitution (Amendment X) all the powers not delegated to the United States by the Constitution or prohibited by it to the states are reserved to the states respectively or to the people. Accordingly, therefore, all sovereign power is in the states and the people. All powers not expressly given to the United States and not forbidden by the Constitution to the states remain in the states and the people.

The same, however, is not true of territories, as the Supreme Court said in *Snow v. United States*⁹:

“The government of the Territories of the United States belongs, primarily, to Congress; and, secondarily, to such agencies as Congress may establish for that purpose. During the term of the pupilage as Territories, they are mere dependencies of the United States. Their people do not constitute a sovereign power. All political authority exercised therein is derived from the General Government.

* * * * *

* * * Strictly speaking, there is no sovereignty in a Territory of the United States but that of the United States itself.”

Again, in *First Nat. Bank of Brunswick v. Yankton*,¹⁰ the court said:

“* * * The Territories are but political subdivisions of the outlying dominion of the United

⁹85 U.S. 317, 21 L. ed. 784, 785 (1873).

¹⁰101 U.S. 129, 25 L. ed. 1046, 1047 (1880).

States. They bear much the same relation to the General Government that counties do to the States, and Congress may legislate for them as States do for their respective municipal organizations. The organic law of a Territory takes the place of a constitution, as the fundamental law of the local government. It is obligatory on and binds the territorial authorities; but Congress is supreme and, for the purposes of this department of its governmental authority, has all the powers of the People of the United States, except such as have been expressly or by implication reserved in the prohibitions of the Constitution.

* * *

* * * In other words, it [Congress] has full and complete legislative authority over the People of the Territories and all the departments of the territorial governments. It may do for the Territories what the People, under the Constitution of the United States, may do for the States."

To the same effect are the following cases:

Late Corporation of Latter-Day Saints v. United States, 136 U.S. 1, 34 L. ed. 478 (1890);

United States v. Winans, 198 U.S. 371, 49 L. ed. 1089, 1093 (1905);

De Lima v. Bidwell, 182 U.S. 1, 45 L. ed. 1041, 1056 (1901);

Downes v. Bidwell, 182 U.S. 244, 45 L. ed. 1088, 1099 (1901);

Assessor v. Com. Cable Co., 16 Haw. 396 (1905);

Christianson v. King County, 239 U.S. 356, 60 L. ed. 327, 331 (1915).

And the same has been recognized by the Supreme Court of the Territory of Hawaii in *Makainai v. Goo Wan Hoy*:¹¹

“* * * The state, being an independent sovereignty within its sphere, makes its own constitution and laws, creates its own courts and fixes their jurisdiction; while a territory, being a political dependency under the absolute control and dominion of Congress, its organic law is made by Congress and its courts and their jurisdiction and procedure is defined by the same power. *First National Bank v. Yankton*, 101 U.S. 129; *Patterson v. Gile*, 1 Colo. 200.”

2. Congress has never delegated to the Territory of Hawaii the power to tax the United States or its agencies or instrumentalities.

The basic grant of power to the Territory giving it the right to impose taxes of any kind is contained in Section 55 of the Hawaiian Organic Act as amended (April 30, 1900, 31 Statutes at Large, 141, Ch. 339), and is contained in the following words of said section:

“That the legislative power of the Territory shall extend to all rightful subjects of legislation not inconsistent with the Constitution and laws of the United States locally applicable.”

Under this broad legislative power, the Territory has not purported to tax the United States or its agencies or instrumentalities, nor has it attempted to tax the privilege of making sales to the United States, its agencies or instrumentalities, until January 1, 1942.

¹¹14 Haw. 607, 609 (1903).

We contend that this interpretation of the constitutional taxing power of the Territory as administered by the Territory until the end of 1941 is correct, and that there is no basis for any change in 1942 in the absence of any congressional action consenting to such tax or even of action by the Legislature of the Territory of Hawaii.

Congress has not since 1900 enlarged the legislative power of the Territory, and for over forty years the Territory has recognized that it did not have the power to tax with regard to the proceeds of sales here in question. The Organic Act, which is in effect the Constitution of the Territory, must be interpreted in the light of the conditions under which it was enacted. No different interpretation can be given to it by reason of a changed concept with regard to states' powers that arises by reason of later judicial interpretation, and does not arise out of additional grants of power. In the case of states, states do have all sovereign power, and when the courts change their decisions with regard to states' powers they are merely interpreting and defining what that sovereign power consists of and to what extent the sovereign power of the states was cut into and limited by the Constitution in favor of the United States.

In the case, however, of the Territory's power to tax, court decisions relative to the states have no application because the territories have only such powers as are given them by Congress and the power that is given them by Congress depends upon what Congress thought it was granting at the time of the enactment

of the power granting act. The Organic Act of the Territory of Hawaii is the Constitution of the Territory, and as such must be interpreted in the light of its meaning and intent when Congress adopted it. Such is the recognized rule with regard to a constitution or fundamental grant of power to a government. In the case of *Dred Scott v. Sanford*,¹² the question before the court was whether negroes were citizens. The court found that they were not included and were not intended to be included under the word "citizens" in the Constitution and could, therefore, claim none of the rights and privileges which that instrument provides for and secures to the citizens of the United States. On the contrary, they were at that time considered as a subordinate and inferior class of beings, who had been subjugated by the dominant race, and whether emancipated or not, yet remained subject to their authority, and had no rights or privileges but such as those who held the power and the government might choose to grant them. The court said at page 700:

"It is not the province of the court to decide upon the justice or injustice, the policy or impolicy of these laws. The decision of that question belonged to the political or law-making power; to those who formed the sovereignty and framed the Constitution. The duty of the court is to interpret the instrument they have framed, with the best lights we can obtain on the subject, and to administer it as we find it, according to its true intent and meaning when it was adopted."

¹²60 U.S. 393, 15 L. ed. 691 (1857).

Page 709:

“No one, we presume, supposes that any change in public opinion or feeling, in relation to this unfortunate race, in the civilized nations of Europe or in this country, should induce the court to give to the words of the Constitution a more liberal construction in their favor than they were intended to bear when the instrument was framed and adopted. Such an argument would be altogether inadmissible in any tribunal called on to interpret it. If any of its provisions are deemed unjust, there is a mode prescribed in the instrument itself by which it may be amended; but while it remains unaltered, it must be construed now as it was understood at the time of its adoption. It is not only the same in words, but the same in meaning, and delegates the same powers to the government, and reserves and secures the same rights and privileges to the citizen; and as long as it continues to exist in its present form, it speaks not only in the same words, but with the same meaning and intent with which it spoke when it came from the hands of its framers, and was voted on and adopted by the people of the United States. Any other rule of construction would abrogate the judicial character of this court, and make it the mere reflex of the popular opinion or passion of the day. This court was not created by the Constitution for such purposes. Higher and graver trusts have been confided to it, and it must not falter in the path of duty.”

Again, in *South Carolina v. United States*:¹³

“The Constitution is a written instrument. As such its meaning does not alter. That which it

¹³199 U.S. 437, 50 L. ed. 261, 264 (1905).

meant when adopted, it means now. Being a grant of powers to a government, its language is general; and, as changes come in social and political life, it embraces in its grasp all new conditions which are within the scope of the powers in terms conferred. In other words, while the powers granted do not change, they apply from generation to generation to all things to which they are in their nature applicable. This in no manner abridges the fact of its changeless nature and meaning. Those things which are within its grants of power, as those grants were understood when made, are still within them; and those things not within them remain still excluded. As said by Mr. Chief Justice Taney in *Scott v. Sandford*, 19 How. 393, 426, 15 L. ed. 691, 709:

‘It is not only the same in words, but the same in meaning, and delegates the same powers to the government, and reserves and secures the same rights and privileges to the citizen; and as long as it continues to exist in its present form, it speaks not only in the same words, but with the same meaning and intent with which it spoke when it came from the hands of its framers, and was voted on and adopted by the people of the United States. Any other rule of construction would abrogate the judicial character of this court, and make it the mere reflex of the popular opinion or passion of the day.’ ”

The question immediately arises as to what Congress thought it was delegating to the Territory at the time of the passage of the Organic Act. A general

statement of the law in this respect is set out in *Domenech v. National City Bank*:¹⁴

“* * * Puerto Rico, an island possession like a territory, is an agency of the federal government, having no independent sovereignty comparable to that of a state in virtue of which taxes may be levied. Authority to tax must be derived from the United States. But like a state, though for a different reason, such an agency may not tax a federal instrumentality. A state, though a sovereign, is precluded from so doing because the Constitution requires that there be no interference by a state with the powers granted to the federal government. A territory or a possession may not do so because the dependency may not tax its sovereign. True the Congress may consent to such taxation; but the grant to the Island of a general power to tax should not be construed as a consent. Nothing less than an act of Congress clearly and explicitly conferring the privilege will suffice. * * *”

In *Posadas v. National City Bank*,¹⁵ the court referred to the controlling rule of the *Domenech* case that “a dependency may not tax the sovereign.”

Congress has not specifically consented to any tax by the Territory on sales to the United States or its agencies or instrumentalities.

In *Puerto Rico v. Shell Co.*,¹⁶ the court, discussing the *Domenech* case, said that it there held that the grant to the Territory of the general power to tax

¹⁴294 U.S. 199, 79 L. ed. 857, 861 (1935).

¹⁵296 U.S. 497, 80 L. ed. 351, 354 (1936).

¹⁶302 U.S. 253, 82 L. ed. 235, 247 (1937).

did not constitute consent on the part of Congress that a tax not authorized by the statute in question could be laid.

In granting legislative power to the Territory, including the general power to tax, it is neither desirable nor probable that Congress would leave the limits of the power to tax as vague and undefined as would result from having the applicability of any tax vary with every judicial interpretation and dictum of the Supreme Court. As was stated in *Helvering v. Griffiths*:¹⁷

“* * * Such an intention [to have the coverage of a tax vary with judicial changes] would be a serious departure from the usual policy of Congress to provide the taxpayers and tax-gatherers with a practical basis for the timely settlement of questions of taxation arising each year. * * *”

Similarly, in *E. V. Parker v. Motor Boat Sales, Inc.*:¹⁸

“* * * An interpretation [or a jurisdictional proviso of a statute] which would enlarge or contract the effect of the proviso in accordance with whether this Court rejected or reaffirmed the constitutional basis of the Jensen and its companion cases cannot be acceptable. * * *

* * * Without affirming or rejecting the *constitutional*¹⁹ implications of those cases, we accept them as the measure by which Congress intended to mark the scope of the Act they brought into existence.”

¹⁷318 U.S. 371, 87 L. ed. 843, 861 (1943).

¹⁸314 U.S. 244, 249, 86 L. ed. 184 (1941).

¹⁹Italics the court's.

The *Griffiths* case stands squarely for the proposition that Congress may and does incorporate current constitutional rules into its legislation by implication; that the courts will support such incorporation and that the policy of stability of a law militates in favor of such incorporation and against the inference of vacillating and undefined contraction of the tax with subsequent varying decisions.

3. **A statute which includes the gross receipts from sales to the United States or its agencies or instrumentalities, within the measure of the tax, is a tax on the United States.**

With regard to the power of the Territory to impose a tax on account of sales to the United States, the court below, in its majority opinion, stated: "A tax imposed by a non-federal political agency, however reasonable, universal and non-discriminating, the legal effect of which is to lay a direct and immediate tax upon the instrumentalities of the United States, is within the implied power of the Constitution of the United States against laying a burden upon or interfering with federal activities, even though imposed under the guise of an excise tax. A nondiscriminating territorial excise tax, measured by the application of rates against values, gross proceeds of sales or gross income, as the case may be, is not within the constitutional prohibition merely because in its incidence it might indirectly reach a federal instrumentality." (R. 193-4). "The tax the legality of which is in question herein was assessed for the year 1942. The *King & Boozer* case was decided in November, 1941. And the rationale of the *King & Boozer* case applies without

the necessity of further legislation on the subject.” (R. 195).

The minority opinion, concurring in part, holds that the effect of the cases of *James v. Dravo Contracting Co.*, *supra*, *Alabama v. King & Boozer*, *supra*, *Curry v. United States*, *supra*, *Penn Dairies v. Milk Control Com.*,²⁰ is that from the time of the enactment of the General Excise Tax Law, the meaning of the Constitution, as construed by the Supreme Court of the United States, underwent a complete change with regard to the exemption from nondiscriminatory taxation by a state of federal sales, so that after 1941 such sales were held to be rightful subjects of nondiscriminatory taxation and no longer exempt therefrom under the Constitution. This construction was stated to be decisive in the minority opinion.

Both the majority and minority opinions agree that the *Panhandle* line of cases constituted the controlling rule of 1935 with regard to the taxability of sales to the United States. Both agree, likewise, that a state, and, therefore, a territory, cannot directly burden the activities of the Federal Government. Both, however, fail to see that the direct holding of the *Panhandle* line of cases that a state may not tax the proceeds of sales to the Federal Government still is controlling because such cases have not been overruled in their direct holding that a state may not impose a tax on sales to the United States, and for the further reason that a tax on sales to the United States is a direct interference with the government activity of purchas-

²⁰318 U.S. 261, 87 L. ed. 748 (1943).

ing what it requires in the exercise of its governmental functions and is, therefore, in violation of the Federal Government's implied immunity from tax under the Constitution.

4. **The Panhandle line of cases has not been overruled in so far as it holds that a tax on account of sales to the United States is unconstitutional.**

The *Panhandle Oil* case *supra* involved a privilege tax on all persons engaged in distributing gasoline, measured on a per gallon basis. The issue was the right to collect such tax on account of sales of gasoline to the United States. The court held that the state may not burden or interfere with the exertion of the national power or make it a source of revenue or tax the means used in performance of federal functions; that the right of the United States to make purchases is derived from the Constitution; that the petitioner's right to make sales to the United States is not given by the state and does not depend on state law; that it results from the authority of the national government under the Constitution to choose its own means and sources of supply; that while the state may impose a charge on the dealer for the privilege of carrying on a trade that is subject to the power of the state, it may not lay a tax on the transactions by which the United States secures the things desired for its governmental purposes; that it is immaterial that the seller is required to report the sales and make the payments thereon; that the sale and purchase constitute a transaction on which the tax is measured and on which the burden rests; that the amount of money claimed

by the state rises and falls precisely as does the quantity of gasoline secured by the Government; that the necessary operation of the enactment is directly to retard, impede and burden the exertion by the United States of its constitutional power of operating a fleet; and that to use the number of gallons sold to the United States as a measure of a privilege tax is to tax the sale itself.

In *Indian Motorcycle Co. v. United States*, *supra*, there was involved a United States tax on motorcycles sold to a municipal government. In holding such sales to be immune from tax in order to preserve our constitutional system of dual government, the court quoted from the *Panhandle* case, *supra*, to the effect that the sale and purchase constitute a transaction by which the tax is measured and on which the burden rests.

In *Graves v. Texas Co.*, *supra*, that principle was reiterated in a case involving a tax on storage of gasoline measured by withdrawals in which it was held that the storage was so essential to sale as to be a tax on the sale itself.

The court below held that these cases are no longer applicable to the present case because of the later holdings of the United States Supreme Court cited *supra*. It is appellant's contention that the United States Supreme Court recognized differences between the later cases limiting immunity from tax and the *Panhandle* line of cases, and that the *Panhandle* line of cases still controls in the present case. This is evident from statements made in each of said cases

showing that the transactions there involved have tax implications different from those arising out of the transaction of sale and purchase subjected to tax in the *Panhandle* line of cases.

In *James v. Dravo Contracting Co.*, *supra*, there was involved a gross receipts tax on account of the proceeds of a contract with the United States. The court said of the tax that it was not on the Government, its property or officers, nor on an instrumentality of the United States; that it was nondiscriminatory, and was *not on a contract of the Government*.²¹ The court said that the *Panhandle* and *Indian Motorcycle* cases may be distinguished and must be deemed to be limited to their particular facts. Obviously, the most particular fact of those cases to which the court had reference was that in the *Panhandle* line of cases, the tax was imposed on account of sales to the Government. With regard to direct sales to the Government that much of the case remains the law after the *James v. Dravo* case. The gist of the *Dravo* case is that the mere fact that the gross receipts tax on a contractor with the Government may increase the cost to the Government, nevertheless, that is not a direct enough burden on the Government to invalidate the tax.

In *Alabama v. King & Boozer*, *supra*, where a contractor was required to pay a tax on account of his purchases, the court said that the *Panhandle* line of cases were overruled in so far as they hold that a tax, the economic burden of which falls on the Govern-

²¹Emphasis supplied.

ment, may not constitutionally be imposed by a state. In other words, it is not merely the fact that the economic burden fell on the Government which invalidated the tax in the *Panhandle* line of cases, but primarily it was that the tax was on a transaction in which the Government is a party, so that the tax was directly imposed on an activity of the Federal Government. That this is the meaning of that case can be seen from the fact that the bulk of the decision in *Alabama v. King & Boozer* is concerned with showing that the legal effect of the transaction subject to tax was to obligate the contractor to pay for the lumber, and that it was the contractor that was the purchaser and not the United States. The transaction on account of which the tax was imposed was, therefore, between a seller of lumber and a purchaser who was a cost-plus contractor with the United States, but not an agency or instrumentality of the United States. Although the contractor was bound to deliver the lumber to the Government after the purchase and to be reimbursed, the court was of the opinion that this did not spell immunity because the contractors were, in a loose and general sense, acting for the United States. In its reasoning, this indicates that the court recognized that were the tax on a sale to the Government, or to a Government agency direct, the tax would not have been valid under the holdings of the *Panhandle* line of cases.

Curry v. United States, supra, likewise does not determine that sales to the United States are subject to tax. There was involved a use tax on materials pur-

chased by a cost-plus contractor and appropriated to its contract with the Government. The court pointed out that the contractor was not an agent or instrumentality of the Government, and that the tax only affects the Government as the economic burden is shifted to it through operation of a contract. The transactions involved in both the *King & Boozer* and *Curry* cases are a step further removed from the transaction involved in the *Panhandle* line of cases and the present case. In the case of cost-plus contractors in the *King & Boozer* and *Curry* cases, it is the purchase and use of materials by the contractor who is not the agent or instrumentality of the United States that is the subject matter of the case. In the *Panhandle* line of cases, as in the present case, it is the acquisition of property by the Government, in effect, that was taxed, even though the tax was laid on the seller.

The case of *Penn Dairies v. Milk Control Com.*, *supra*, does not advance the Territory's case much further. In that case there was involved the validity of minimum price regulations of the state as applied to the sale of milk by a dealer to the United States. The court held in upholding a local law under the police power of the state that those who furnish supplies or render services are not agencies and do not perform governmental functions, and that, although the regulation imposes an economic burden on the Government, there is no greater impairment of a federal right than a tax on sales to contractors with the United States. The statement in that case, with regard to certain regulations of the War Department,

that they rest on the reasoning of the *Panhandle Oil* and like cases which were overruled as in *Alabama v. King & Boozer*, refers to the reasoning of those cases that a tax is invalid merely because the burden may be shifted to the United States. A reference back to the *King & Boozer* case will show that this is what the court meant. There the court said that the asserted right of one (referring to the Federal and State Governments as separate sovereign powers within the same territorial jurisdiction) to be free of taxation by the other does not spell immunity from paying the additional costs attributable to the taxation of those who furnish supplies to the Government and who have been granted no tax immunity, and that so far as a different view has prevailed, see *Panhandle* and *Graves* cases, we think it is no longer tenable.

In addition to these cases, there are a number of later cases in which the Supreme Court made statements showing that in each case it recognized that it was dealing with a transaction different than that subjected to tax in the *Panhandle* line of cases. In *Mayo v. United States*,²² the court, in invalidating a tax on activities of the United States, said that they were not dealing, as in *Graves v. New York*,²³ with a tax on the salary of an employee of the Government, or, as in the *King & Boozer* case, with a tax on purchases of a supplier of the United States, or as in the *Penn Dairies* case, with price control of a contractor with the United States.

²²319 U.S. 441, 87 L. ed. 1504 (1943).

²³306 U.S. 466, 83 L. ed. 927 (1939).

In *United States v. County of Allegheny*,²⁴ the court characterized the *Dravo* case as concerned with a tax on the benefits of a contractor from dealings with the United States, the *Graves* case as a tax on salaries received from it, and said of the *King & Boozer* case that the fact that materials were destined to be furnished to the Government does not exempt them from a sales tax imposed on the contractor's vendors.

A case which is much closer to the present case than the *King & Boozer* and *Curry* cases is that of *United States v. County of Allegheny, supra*. In that case there was in question the validity of an *ad valorem* tax imposed on a lessee of the Federal Government measured, in part, by property owned by the Government. This tax was held invalid as an undue interference with the Government's ownership of its property. This is but slightly different from the present case, which is an attempted interference with the Government's acquisition of property in the performance of its governmental functions. In this connection, also, it is interesting to note Mr. Justice Roberts' comment in the minority holding at page 1223 to the effect that the doctrine of immunity from consequent burden on the Government is being reimported into our jurisdiction. However, it is not necessary to rely on the doctrine of immunity from consequent burden on the Government, because, in the present case, the burden is directly on the Government and the tax is directly on a governmental activity.

²⁴322 U.S. 174, 88 L. ed. 1209 (1944).

As was said in the *Indian Motorcycle Co.* case, the sale and purchase constitute a single transaction in which the purchaser is an essential part. No sale is possible without a purchaser and any tax arising out of that transaction is a tax on the purchaser.

In the *Panhandle Oil* case, the court said that the right of the United States to make purchases is derived from the Constitution, and the taxpayer's right to make sales to the United States is not given by the states, nor dependent upon state laws, but results from the authority of the national government under the Constitution to choose its own means and source of supply. While the state may impose a charge for the privilege of carrying on trade, no tax may be laid on transactions by which the United States secures the things desired for Government purposes. Such a tax directly retards, impedes and burdens the execution by the United States of its constitutional powers.

In *McLeod v. Dillworth Co.*,²⁵ the court characterized a sales tax as a tax on the freedom of purchase; a freedom which war-time restrictions served to emphasize; and, in *Freeman v. Hewitt*,²⁶ in discussing the Indiana Gross Income Tax, on which the Territorial General Excise Tax was modeled, said that a tax on the sale itself is no different than a tax on gross receipts, and that a tax on gross receipts is a direct imposition on the freedom of commercial flow of goods.

²⁵322 U.S. 327, 330, 88 L. ed. 1305, 1307 (1944).

²⁶329 U.S. 249, 91 L. ed. (Adv. Sheets) 205, 210 (1946).

In *Richfield Oil Corp. v. State Board of Eq.*,²⁷ where there was involved the validity of a tax on exports, the court said that the issue turns not on the characterization which the state gives the tax, but on its operation and effect. The incident giving rise to the tax was the passage of title and the completion of sale, which is a part of the export process.

Incidentally, it is apparent now, after the case of *United States v. County of Allegheny*, *supra*, that it is not necessary that the tax be imposed on the Government itself in order that the transaction in which the Government is a party shall be immune, and that a tax is not necessarily valid if laid upon a third party even though the burden falls on the Government.

The test of validity of state taxes on account of transactions with the Federal Government, seems to be the degree of directness of the imposition of the tax; that is, if the tax is imposed against the Government or its instrumentalities or agencies, or against its officers as such, or upon its property, or upon a contract of the Government, or upon its acquisition of property, then the interference with the functions of the Federal Government is too direct an interference with its sovereignty. If, on the other hand, the tax is imposed upon the proceeds of a contract with the United States, as in *James v. Dravo Contracting Co.*; upon the purchases of a supplier of the United States, as in the *King & Boozer* case; or on the use of materials purchased by a contractor with the United

²⁷329 U.S. 69, 91 L. ed. (Adv. Sheets) 123, 131, 132 (1946).

States which are appropriated by the contractor to the contract with the United States, as in *Curry v. United States*; or if control is exercised over a contractor with the United States, as in the *Penn Dairies* case; then, the interference with a federal function is not so direct as to constitute an undue interference with the sovereignty of the United States.

An examination of the fundamental basis for federal immunity from state taxation shows that there is not the same reason to cut down on the immunity in the cases of territories as there is in the case of states. The reason for whittling away the doctrine of federal immunity from state taxation is the importance of preserving the sovereignty of states which under the Constitution is reserved to the states. As pointed out above, there is no sovereignty in the Territory and the basic reason for allowing some interference with federal functions disappears. The court, in cases in which the imposition of a state tax was justified even though it burdened the Federal Government, stated that this was necessary in order to preserve the dual sovereignty provided for by the Constitution.

In *Union Pacific R. R. Co. v. Peniston*,²⁸ the nature of the dual sovereignty contemplated by the Constitution was discussed. The court said, in part:

“That the taxing power of a State is one of its attributes of sovereignty; that it exists independently of the Constitution of the United States, and underived from that instrument; and

²⁸85 U.S. 5, 21 L. ed. 787, 791 (1873).

that it may be exercised to an unlimited extent upon all property, trades, business and avocations existing or carried on within the territorial boundaries of the State, except so far as it has been surrendered to the Federal Government, either expressly or by necessary implication, are propositions that have often been asserted by this court. And in thus acknowledging the extent of the power to tax belonging to the States, we have declared that it is indispensable to their continued existence. No one ever doubted that before the adoption of the Constitution of the United States, each of the States possessed unlimited power to tax, either directly or indirectly, all persons and property within their jurisdiction, alike by taxes on polls, or duties on internal production, manufacture or use, except so far as such taxation was inconsistent with certain treaties which had been made. * * *

There are, we admit, certain subjects of taxation which are withdrawn from the power of the States, not by any direct or express provision of the Federal Constitution, but by what may be regarded as its necessary implications. They grow out of our complex system of government, and out of the fact that the authority of the National Government is legitimately exercised within the States. While it is true *that* government cannot exercise its power of taxation so as to destroy the state governments, or embarrass their lawful action, it is equally true that the States may not levy taxes the direct effect of which shall be to hinder the exercise of any powers which belong to the National Government. The Constitution

contemplates that none of those powers may be restrained by state legislation. * * * The States are, and they must ever be, co-existent with the National Government. Neither may destroy the other. Hence the Federal Constitution must receive a practical construction. Its limitations and its implied prohibitions must not be extended so far as to destroy the necessary powers of the States, or prevent their efficient exercise.”

Again, in *Graves v. New York*,²⁹ the court said:

“So much of the burden of a nondiscriminatory general tax upon the incomes of employees of a government, state or national, as may be passed on economically to that government, through the effect of the tax on the price level of labor or materials, is but the normal incident of the organization within the same territory of two governments, each possessing the taxing power. The burden, so far as it can be said to exist or to affect the government in any indirect or incidental way, is one which the Constitution presupposes, and hence it cannot rightly be deemed to be within an implied restriction upon the taxing power of the national and state governments which the Constitution has expressly granted to one and has confirmed to the other. The immunity is not one to be implied from the Constitution, because if allowed it would impose to an inadmissible extent a restriction on the taxing power which the Constitution has reserved to the state governments.”

²⁹306 U.S. 466, 83 L. ed. 927, 937 (1939).

It is apparent from these extracts that it is necessary to permit states to interfere to some extent with federal powers by taxation because the states must co-exist with the national government and the power to tax is essential to the continued existence of states.

The court below appears to believe that because the states' power to tax transactions involving the United States has been expanded, the same thing has happened in the case of the Territory's right to tax. This, however, does not follow, since the expansion of the states' right to tax depends upon the existence of two sovereigns within the same field, each of which is entitled to tax, and each of which is entitled to be free from interference by the other, and the court has determined that the right to tax is, in some instances, a justifiable reason for some interference in the exercise of the sovereign rights of the other. No such problem, however, arises in the case of a territory which is not a sovereign and which derives all its powers from the Federal Government. Its right to tax, therefore, must be subservient to the sovereign's right to be free of any interference by its artificially created subsidiary except to the extent that it has given its consent to such a tax, or to such interference with the sovereign's powers and actions.

B. THE TERRITORY OF HAWAII CANNOT LAWFULLY IMPOSE A TAX AT A HIGHER RATE WITH RESPECT TO SALES TO POST EXCHANGES THAN WITH RESPECT TO SALES TO OTHER RETAIL MERCHANTS FOR RESALE.

Appellant contends that for the reasons set forth above, the Territory cannot lawfully impose a tax on the gross proceeds of sales to the United States or to any federal agency or instrumentality, including post exchanges. It is the further contention of appellant that in the event it is held that such taxes can validly be imposed, in no event can the gross proceeds of sales to post exchanges be taxed at more than $\frac{1}{4}$ of 1%, which is the rate imposed with respect to sales to other retailers for resale and not for consumption.

There seems to be no dispute as to the general principle of law that a state or territorial tax, measured by gross proceeds of sale, must be nondiscriminatory in so far as said agencies are concerned in order to be outside the constitutional prohibition.

The United States Supreme Court, in a number of cases in which state taxes imposed with regard to gross receipts from contracts with the United States have been held valid, has said that the tax must be nondiscriminatory in so far as the Federal Government is concerned. That is, even where the state is permitted to indirectly burden agencies of the Federal Government in order to permit the state to continue its existence through the exercise of its sovereign power to tax, the court has asserted that the burden on the Government must not be greater than

that on other taxpayers within the state. For example, in the *Dravo* case, *supra*, the court said:

“* * * Respondent has no constitutional right to immunity from *nondiscriminatory*³⁰ local taxation and the mere fact that the tax in question burdens respondent is no defense. * * *”

Again, in the *King & Boozer* case, *supra*, the court said:

“* * * So far as such a *nondiscriminatory*³⁰ state tax upon the contractor enters into the cost of the materials to the Government, that is but a normal incident of the organization within the same territory of two independent taxing sovereignties. * * *”

And again, in the *Penn Dairies* case, *supra*, the court said:

“* * * and the mere fact that *nondiscriminatory*³⁰ taxation or regulation of the contractor imposes an increased economic burden on the government is no longer regarded as bringing the contractor within any implied immunity of the government from state taxation or regulation. * * *”

These cases, in laying down the general rule that there is no implied constitutional immunity of the Government and its agencies from nondiscriminatory state taxation upon persons dealing with them merely because the economic burden thereof may be shifted to the Government, by necessary implication must be taken to mean that there is an implied constitu-

³⁰Emphasis supplied.

tional immunity from discriminatory state taxation. It follows that any discriminatory tax directly impedes, retards and burdens the constitutional exercise of the powers of the Government in the performance of its functions, and is unconstitutional.

In determining that the Territory could impose a tax at the rate of $1\frac{1}{2}\%$ on account of sales to post exchanges, the court below determined:

(1) That the statute required the imposition of the tax at $1\frac{1}{2}\%$ rather than $\frac{1}{4}$ of 1% because appellant, with respect to sales to post exchanges, was not a wholesaler within the meaning of the Act;

(2) That the classification under which sales to post exchanges are taxed at a higher rate than sales to other retailers for resale, is a natural and reasonable classification of vendors, and, therefore, not discriminatory; and

(3) That factually no discrimination exists against sales to post exchanges.

With regard to the first determination, appellant contends that in so construing the General Excise Tax Law the court below has committed such manifest error and has so clearly departed from ordinary legal principles, and is so clearly wrong in selecting the construction chosen, that this Court, on appeal, is not bound to follow its conclusions, but may itself determine the meaning of the law.³¹ Appellant further contends that if this Court is bound by the construc-

³¹*Waialua Agricultural Co. v. Christian*, 305 U.S. 91, 109, 110, 83 L. ed. 60, 71, 72 (1938).

tion placed upon the law by the Territorial Supreme Court, then the different tax treatment on account of sales to post exchanges as compared to sales to other retailers for resale constitutes a discrimination which would invalidate the Act. Further, appellant contends that factually the discrimination is so clear as to leave no room for question, and that considering the practical effects of the taxing statute, there is such an unreasonable burden placed upon sales to post exchanges as to make the tax unconstitutional.

1. **The General Excise Tax Law properly construed does not impose a tax at a higher rate with respect to sales to post exchanges than with respect to sales to other retailers.**

The reclassification of appellant with regard to his sales to post exchanges and the imposition of the tax with regard to those sales as retail sales at the rate of $1\frac{1}{2}\%$ rather than as wholesale sales at the rate of $\frac{1}{4}$ of 1% is justified by the Territory under the provisions of Sec. 1 (10), (12) and (13) of the General Excise Tax Law, which reads in part as follows:

“Section 1. *Definitions.* When used in this Act, unless otherwise required by the context:

* * * * *

(10) ‘Wholesaler’ or ‘jobber’ shall apply only to a person doing a regularly organized whole-sale or jobbing business, known to the trade as such, and only with respect to the following sales: (a) sales, to a licensed retail merchant or jobber, for purposes of resale; * * *

‘Wholesaler’ or ‘jobber’ shall mean a person, or a definitely organized division thereof, definitely organized to render and rendering a gen-

eral distribution service which buys and maintains at his or its place of business a stock or lines of merchandise which he or it distributes; and which, through salesmen, advertising or sales promotion devices, sells to licensed retailers, or to institutional, or licensed commercial or industrial users, in wholesale quantities and at wholesale rates.

* * * * *

(12) 'Retail' means the sale of tangible personal property, other than by a wholesaler as such within the definition of this Act, for consumption or use by the purchaser and not for resale.

(13) 'Retailer' shall mean any person who sells, other than as a wholesaler within the definition of this Act, tangible personal property for consumption or use by the purchaser and not for resale."

Appellant, in selling tangible personal property to post exchanges, was doing a regularly organized wholesale business, known to the trade as such, and all sales were for the purpose of resale. Such sales were not for consumption or use by the purchaser as such words are restricted by the phrase "and not for resale" in the statutory definition of "retail" and "retailer." However, the purchasing post exchanges, operating exclusively under army regulations of the War Department, were not licensed under the Act. They conducted no business that was subject to tax under the Act. They were not wholesalers, jobbers or consumers, but, as instrumentalities of the United States and arms of the War Department, they, in

the performance of constitutional functions, maintained retail stores, bought for the purpose of resale, and resold at the lowest possible price to the armed forces and civilian employees of the Federal Government on army posts for the consumption or use of such purchasers for their convenience and for additional benefits to the armed forces not otherwise provided by the Government. See *Army Regulations*;³² *Standard Oil Co. of California v. Johnson*;³³ *Federal Land Bank v. Bismarck Lumber Co.*³⁴

In holding that with respect to sales to post exchanges appellant was not a wholesaler within the meaning of the Act, the court determined:

(1) That post exchanges were not merchants since their functions are governmental and not proprietary; and

(2) That sales to post exchanges are not to be regarded as sales subject to the wholesale rate since post exchanges are not licensed as that term is used in Sec. 1 (10) (a) of the General Excise Tax Law.

The word "merchant" is not defined in the Act, and its plain, ordinary and commonly accepted meaning must be taken to be the one intended. "Merchant" is defined in Webster's International Dictionary, Second Edition, as: "One who carries on a retail business; a storekeeper or shopkeeper." A "retail merchant" is a paraphrase of the word "retailer" as defined by the Act, and serves to identify the purchaser

³²No. 210-65 of the War Department.

³³316 U.S. 481, 86 L. ed. 1611 (1942).

³⁴314 U.S. 95, 86 L. ed. 65 (1941).

as a retailer in contradistinction to a wholesaler, jobber or consumer.³⁵

In limiting sales by wholesalers to retailers as the sales to which the wholesale rate is applicable, the Act serves to prevent the lower rate from being applicable in the case of sales by a wholesaler to the consumer. From the facts, it is apparent that post exchanges are retailers, since they carry on retail businesses as retail storekeepers, purchase exclusively as retailers, resell as retailers, and engage in retail activities with the object of economic benefit, either direct or indirect.³⁶ The court below, in its majority opinion, in holding that post exchanges are not merchants, grounded its determination on the fact that as arms of the Government, the functions of the post exchanges are governmental and not proprietary.

As pointed out in *New York v. United States*,³⁷ however, any distinction between "governmental" and "proprietary" is applicable in so far as a state tax imposed on a federal agency is concerned; that the considerations bearing on taxes by the states of the activities of the Federal Government are not correlative with the considerations bearing on federal taxation of state agencies or activities; and that the distinction between "governmental" and "proprietary" interests, stressed in the older cases, is untenable. A territory or state cannot tax post exchanges as retail merchants, not because they perform only govern-

³⁵See dissenting opinion below (R. 218-219).

³⁶See dissenting opinion below (R. 219).

³⁷326 U.S. 572, 90 L. ed. 326 (1946).

mental functions as an incident of their relationship to the Federal Government, but because they are part of a department of the Government, and to tax those parts would interfere with the constitutional exercise of federal powers in which the states and their citizens, as well as the Territory and its citizens, are equally interested.³⁸

In determining whether the appellant, in dealing with post exchanges, acted as a wholesaler under the General Excise Tax Law, it is apparent that all the requirements relative to the nature of a wholesaler's business and the purposes of sale have been fulfilled except for the requirement that the sale must be to a licensed retail merchant or jobber. Post exchanges are admittedly not jobbers. As pointed out above, appellant contends that they are merchants. The court below held that in order to be a "licensed retail merchant" it was necessary that a license, required of all persons subject to gross income tax under the General Excise Tax Law, be taken out; that post exchanges, being constitutionally immune from being required to take out such a license, were, therefore, not licensed as required in the Act; and that, therefore, the seller to post exchanges could not qualify as a wholesaler with respect to such sales. Appellant contends that this is an erroneous construction of the meaning of the word "licensed" as used in the Act, and is a construction which renders the statute unconstitutional.

³⁸See dissenting opinion below (R. 222-223).

As pointed out in the dissenting opinion,³⁹ the court might properly have construed the term "licensed retail merchants" to include post exchanges and thus preserve the constitutionality of the Act. The term "licensed" is not defined in the statute. There is no need to confine its definition to the narrow construction placed thereon by the Territorial Supreme Court based on the strict statutory sense of securing a license under the Act. The term "licensed" could properly be held to apply to a retail merchant who is lawfully permitted by proper authority to carry on a retail business which, without such permission, would be illegal. The plain, ordinary and accepted meaning of the term "license" is "authority or liberty given to do or forbear any act; permission to do something (specified); esp., a formal permission from the proper authorities to perform certain acts or to carry on a certain business which without such permission would be illegal; also, the document embodying such permission. * * *"⁴⁰ The post exchanges come completely within this definition; they have the permission in the form of army regulations of the War Department pursuant to congressional enactments,⁴¹ to carry on retail businesses within the Territory from the United States as the proper authority under the Constitution, the authorized War Department regulations being the document embodying such permission and having the force of law. Any contention of difference between them and other retail

³⁹(R. 234 to 237 inclusive).

⁴⁰Webster's International Dictionary, Second Edition.

⁴¹16 Stat. 315-319; 18 Stat. 337.

merchants would be purely fanciful, and it cannot reasonably be argued that the Legislature ever intended to classify wholesale sales made to retail merchants duly licensed with the Territory by the War Department in accordance with said law under the Constitution differently from those made to retail merchants duly licensed by the Tax Commissioner in accordance with Territorial law under the Act, both purchasers being retailers who are equally law abiding.

Construing the adjective "licensed" in conformity with its plain, ordinary and accepted meaning, the Act is uniform with respect to wholesale sales and operates without discrimination in making applicable the lower rate to the case of a wholesaler. It does so equitably with respect to wholesale sales made to all licensed retail merchants within the Territory, regardless of the source of the purchaser's permission to carry on retail business therein, so long as it is derived from a proper authority and without such permission the conduct thereof would be illegal. Thus construed the Act does not infringe upon or disregard the implied constitutional immunity of purchasing post exchanges engaged in the retail business in the exercise of their right to buy at wholesale within the Territory for purposes of resale. Accordingly, such a tax would be nondiscriminatory.

2. Assuming that the General Excise Tax Law requires the imposition of a higher rate with respect to sales to post exchanges than with respect to sales to other merchants, then said Act is unconstitutional.

The requirement of the statute, as construed by the court below, that a retailer be licensed (that is, required to take out a license under the Act) in order that sales to such retailer be taxed at $\frac{1}{4}$ of 1% rather than at $1\frac{1}{2}\%$, is not a reasonable one. It depends solely on the character of the retailer. The only material respect in which post exchanges differ from other retailers, in the carrying on of their activities, is that post exchanges are not subject to tax by the Territory of Hawaii with respect to sales made by them, since they are agencies or instrumentalities of the United States. That difference, arising from constitutional immunity, cannot be made the basis of a discrimination against them in respect to the purchases they make. The difference in character of sales, on which the rate is based, must have a reasonable relationship to the purpose of the legislation. The fact that in effect the post exchange is an arm of the Government does not justify any difference in taxes on account of purchases made by it. See *Quaker City Cab Co. v. Pennsylvania*,⁴² *Southern R. Co. v. Greene*,⁴³ *Bethlehem Motors Corp. v. Flynt*,⁴⁴ *Concordia Fire Ins. Co. v. Illinois*.⁴⁵

The only reason why the purchasing post exchanges have an unlicensed status under the Act is because

⁴²277 U.S. 389, 72 L. ed. 927 (1928).

⁴³216 U.S. 400, 54 L. ed. 536 (1910).

⁴⁴256 U.S. 421, 65 L. ed. 1029 (1921).

⁴⁵292 U.S. 535, 78 L. ed. 1411 (1934).

they are exempt on their resales from taxation by the Constitution of the United States. It is apparent, therefore, that the constitutional exemption is not disregarded, but, on the contrary, is the basic reason for the higher assessment. In so far as the Supreme Court of the Territory of Hawaii holds that the Act must be construed as imposing a higher tax on sales to post exchanges than on sales to other retailers, the Act must be regarded as attempting to obtain on immediate sale that which would be constitutionally unobtainable on subsequent resale. Such would be the effect notwithstanding the fact that the unlicensed status under the Act of the post exchanges, by reason of constitutional exemption, and what would be the different status of other purchasing retail merchants required to have a license under the Act, have no bearing whatsoever upon their respective purchasing characters in immediate sales to them. Their relative status with respect to being licensed relates wholly to their respective taxable and nontaxable characters under the Act upon subsequent resale, neither status affecting either the right or privilege of purchase. Such would be the effect even though there is no real or substantial difference between their purchasing characters at the time of purchase, their purposes of buying being the same and the nature of their retail purposes substantially the same. This would be so even though there is no reasonable or tenable distinction to be found in the fact that post exchanges exercise their right of purchase under authorized War Department regulations as a constitutional function and other purchasing retail merchants exercise

their privilege of purchase under a license provided by the Act as a proprietary function.⁴⁶

The fact that there appears to be equal treatment under the Act to sales for resale to those exempted by the Act itself, does not serve to remove the discrimination. The Legislature may exempt any otherwise taxable person, and has the power to withdraw the exemption granted at any time within its discretion as dictated by the equitable and economic necessities of the case. The Legislature has with one hand, in effect, extended exemption to certain otherwise taxable persons as well as to public utilities of the Territory and its subdivisions, and, with the other hand, partly withheld the full force of such exemptions. However, it cannot withdraw, nor effectively consent to that which it did not give, nor can it take away any part of an immunity impliedly granted under the Constitution. The considerations with respect to persons exempted by the Act have no relation to those exempted under the Constitution, and the fact that the Act would appear to operate equally with respect to sales to them is immaterial. It is only with respect to the unequal operation of the law as construed toward substantially the same purchasers who were not exempted by the Act that this court should be concerned. The question, therefore, is whether the assessment of the higher rate with respect to sales to post exchanges, which were constitutionally exempt, on resale, when the lower rate is assessed with respect to such other retail merchants

⁴⁶See dissenting opinion below (R. 221).

not so exempt, constitutes a discriminatory tax that directly trespasses upon the immunity impliedly afforded by the Constitution to post exchanges and renders the legislative authority to assess the higher rate unconstitutional and invalid.⁴⁷

In considering this question, the practical operation and effect of the Act under the construction given it by the Supreme Court as at the time of purchase must be determined. It is obvious that the Act would operate to tax gross proceeds of sales to post exchanges at a rate six times as great as that assessed against those to other retail merchants, and, by so doing, would impose upon post exchanges in the exercise of their right of purchase, a relatively greater burden than that upon the others in the exercise of their privilege of purchase. In addition, it would place an excessive burden upon the right of purchase of post exchanges that would not be imposed had they not been clothed with an implied constitutional immunity. It is obvious that the effect thereof directly would tend to discourage sales to post exchanges while encouraging those to other retail merchants. Such treatment would unquestionably be unfair and injurious to post exchanges. It justifies the inference that the Act so construed would be unfair in design, favoring retail businesses within the Territory which are in competition to government retail businesses. Such an ununiform excise tax law is discriminatory in so far as the exercise of the right of purchase by post exchanges is concerned.⁴⁸

⁴⁷See dissenting opinion below (R. 223 to 225 inclusive).

⁴⁸See dissenting opinion below (R. 225).

As stated by the Supreme Court in *New York v. United States, supra*, “* * * ‘discrimination’ is not a code of specific but a continuous process of application * * *” and, as pointed out by Mr. Justice Holmes in his dissenting opinion in the *Panhandle* case, *supra*, “* * * this court which so often has defeated the attempt to tax in certain ways can defeat an attempt to discriminate or otherwise go too far without wholly abolishing the power to tax. The power to tax is not the power to destroy while this court sits. The power to fix rates is the power to destroy if unlimited, but this court while it endeavors to prevent confiscation does not prevent the fixing of rates. * * *”

Thus, discrimination being a continuous process of application, it follows that if the Territory has the power to fix a discriminatory rate with respect to sales to post exchanges substantially higher than with those to other retail merchants, it could fix one still higher and so could the states, thereby effectively expelling post exchanges from territorial and state limits, drying up at its source the necessary flow of merchandise and rendering post exchanges unable to function in defeat of the purpose for which they were created. It is evident therefrom that the power to fix a discriminatory rate is unlimited and hence the power which destroys.⁴⁹ This court should therefore defeat such an attempt to discriminate and prevent the confiscatory assessments from being applied, the pertinent issue under the considered construction

⁴⁹See dissenting opinion below (R. 228).

being whether the assessment made by the tax commissioner would trespass upon the implied constitutional immunity of post exchanges as an immediate or direct interference with the Government's constitutional powers to operate them under the Constitution.⁵⁰

The court below says, with regard to this question, that the question depends on the absorption of the tax by the retailer, and that post exchanges, by reason of their immunity, absorb less in taxes under the General Excise Tax Law than licensed retail merchants in that, in the case of post exchanges, the tax to be absorbed is $11\frac{1}{2}\%$ and, in the case of licensed retail merchants, $13\frac{1}{4}\%$, and that the result is that the purchasers, to whom sales at post exchanges are restricted, as ultimate consumers pay less than the general public purchasing from licensed retail merchants. This reasoning lumps together the taxes imposed on account of two sales; namely, the sale from the wholesaler to the retailer, and the sale by the wholesaler to the consumer. The tax levied on the sale from the wholesaler to the licensed retailer is $\frac{1}{4}$ of 1%, and the tax on the resale by the retailer is $11\frac{1}{2}\%$, making a total of $13\frac{1}{4}\%$.

The very cases relied on by the court below to hold that nondiscriminatory taxes on account of sales to the United States are valid, rest on the reasoning that the ultimate burden of the tax is unimportant. The court below blows hot and cold when it holds that the fact of the burden falling on the Government is

⁵⁰Const., Art. I, Sec. 8.

unimportant in order to sustain the validity of the tax in the first instance, and then argues on the basis of the ultimate absorption of the tax in order to prove that there is no discrimination against the post exchanges. If nothing else, this holding makes clear the purpose of the Territory to collect from the seller to post exchanges a tax at a rate which makes up for the tax on the ultimate retail sale by the post exchange which cannot be levied directly because of the constitutional prohibition.

A rather similar case is that of *Missouri ex rel. Missouri Ins. Co. v. Gehner*,⁵¹ where a state tax was imposed upon all insurance companies measured in part by the net value of all of its assets in excess of the legally required reserve necessary to reinsure its outstanding risks and unpaid policy claims. The question before the court was whether the company could deduct from its return the value of United States bonds owned by it. The court said at page 876:

“* * * It necessarily follows from the immunity created by a Federal authority that a state may not subject one to a greater burden upon his taxable property merely because he owns tax-exempt government securities. Neither ingenuity in calculation nor form of words in state enactments can deprive the owner of the tax exemption established for the benefit of the United States. * * *

* * * * *

“* * * It is clear that the value of appellant's government bonds was not disregarded in making

⁵¹281 U.S. 313, 74 L. ed. 870 (1930).

up the estimate of taxable net values. That is in violation of the established rule. * * *"

That is exactly what has happened in the present case. The tax exemption on sales that would otherwise have afforded an advantage to post exchanges is diminished by imposing a greater tax on account of their purchases. In other words, the Territory, which cannot tax the sales of post exchanges, is attempting to tax their purchases at a higher rate than the tax imposed on similar transactions not involving post exchanges. It is clear that the immunity to tax of sales by the post exchanges was not disregarded in determining the rate of tax payable on account of purchases by them. This is in violation of the established rule that what is immune from tax may not be indirectly taxed in other ways and that the attempt to increase the tax in the manner that the Territory purports to do constitutes undue discrimination against a tax exempt agency or instrumentality.

In any event, it is quite apparent that regardless of any other consideration, it does happen that of all retailers who purchased for resale (with the exception of a few taxpayers exempt from tax on their sales by Territorial law), it is only on the purchases of post exchanges that a higher rate of tax results. That this constitutes a direct interference with federal functions is quite apparent, particularly during war times when the freedom of purchase was substantially restricted by war-time shortages. In the case of post exchanges, because of the imposition of a tax on account of their purchases at a rate six times

as high as that imposed upon purchases of any other purchaser for resale, the court can well understand the difficulties post exchanges would encounter in purchasing what they required to perform their functions. As the United States Supreme Court said in *McLeod v. Dillworth*, *supra*, in characterizing a sales tax on the freedom of purchase, such freedom of purchase is a freedom which war-time restrictions served to emphasize.

CONCLUSION.

It is, therefore, respectfully submitted that:

I. The Territory of Hawaii cannot lawfully impose a tax on the gross receipts from sales to the United States or its agencies or instrumentalities.

(a) The Territory of Hawaii is not a sovereign government with inherent power to impose taxes, but derives its power to tax from the United States.

(b) Congress has never delegated to the Territory of Hawaii the power to tax the United States or its agencies or instrumentalities.

(c) A statute which includes the gross receipts from sales to the United States or its agencies or instrumentalities, within the measure of the tax, is a tax on the United States.

(d) The *Panhandle* line of cases has not been overruled in so far as it holds that a tax on account of sales to the United States is unconstitutional.

II. The Territory of Hawaii cannot lawfully impose a tax at a higher rate with respect to sales to post exchanges than with respect to sales to other retail merchants for resale.

(a) The General Excise Tax Law properly construed does not impose a tax at a higher rate with respect to sales to post exchanges than with respect to sales to other retailers.

(b) Assuming that the General Excise Tax Law requires the imposition of a higher rate with respect to sales to post exchanges than with respect to sales to other merchants, then said Act is unconstitutional.

Dated, Honolulu, T. H.

November 15, 1947.

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No. 11,688

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

THOMAS H. BRODHEAD, doing business
as T. H. Brodhead Co.,

Appellant,

VS.

WILLIAM BORTHWICK, Tax Commis-
sioner and Tax Collector of the Ter-
ritory of Hawaii,

Appellee.

Upon Appeal from the Supreme Court of the
Territory of Hawaii.

BRIEF FOR APPELLEE.

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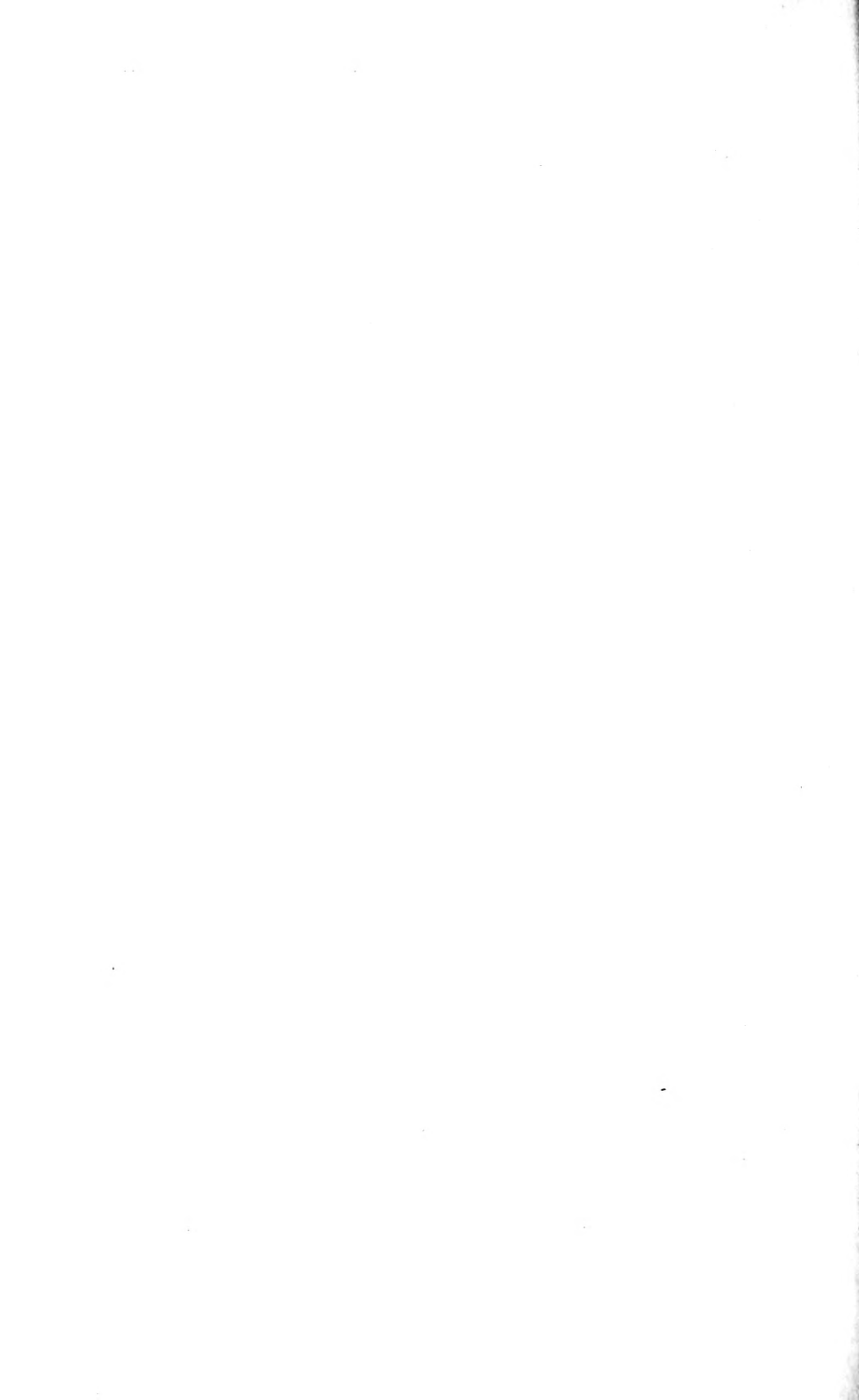
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No. 11,688

IN THE

United States Circuit Court of Appeals
For the Ninth Circuit

THOMAS H. BRODHEAD, doing business
as T. H. Brodhead Co.,

Appellant,

VS.

WILLIAM BORTHWICK, Tax Commis-
sioner and Tax Collector of the Ter-
ritory of Hawaii,

Appellee.

Upon Appeal from the Supreme Court of the
Territory of Hawaii.

BRIEF FOR APPELLEE.

JURISDICTIONAL STATEMENT.

This is an appeal pursuant to section 128 of the Judicial Code (28 U.S.C.A. 225) from a final decision and judgment of the Supreme Court of Hawaii (R. 186-190). Appellant contends that the Constitution and the Hawaiian Organic Act are involved (Complaint Par. VII, R. 5-8). The value in controversy, exclusive of interest and costs, exceeds \$5000; appellant sued to recover taxes in excess of that amount, paid under protest, and recovered nothing. (R. 9, 101, 107.)

STATEMENT OF THE CASE.

Appellant's statement of the case ignores the decision and judgment of the trial court (R. 98-108), affirmed by the Supreme Court (R. 186-190). Appellant's statement consists largely of facts not found, because deemed by the lower court to be immaterial. Some of these facts, by reason of abandonment by appellant of assignments of error 2, 3, 4, 16, and 18 (R. 253-257) through failure to specify them in the brief (Br. 12-15)¹ incontrovertibly are immaterial.² As for

¹The below schedule shows the extent to which the assignments of error have been preserved in the specification of errors.

Assignment of Errors (R. 253-258) No.	Specification of Errors (Br. 12-15) No.
1	1
2	Abandoned
3	Abandoned
4	Abandoned
5	2
6	3
7	4
8	5
9	6
10	7
11	8
12	9
13	10
14	12
15	11
16	Abandoned
17	13
18	Abandoned
19	14
20	15
21 (re specific exemption in the tax law)	Abandoned
21 (re power of the Legislature)	16
22	17

²Among the assignments of error abandoned are numbers 2, 3, 4 and 16, which sought to interpret the statute on the basis of, or give

appellant's statement that he filed gross income tax returns "in all respects as required by the General Excise Tax Law" (Br. 3) that of course is an issue of law in controversy; the statement above quoted is from appellant's complaint (R. 3).

Appellee herewith presents his own statement of the case.

This is a controversy between the appellant-taxpayer and the appellee-tax commissioner. Neither the United States nor any officer or representative of the post exchanges or ships' service stores has appeared in the controversy in any of its stages, as an *amicus curiae* or otherwise. During the period in question appellant correctly returned the amounts of his gross proceeds of sales but (1) claimed for certain of the gross proceeds so disclosed an exemption disallowed by the appellee-tax commissioner, and (2) as to part of the gross proceeds claimed to be exempt, reported the amounts on a line of the return form which would cause the applicable tax rate to be $\frac{1}{4}$ of 1%, if the exemption were disallowed; these amounts were reclassified by the appellee-tax commissioner as taxable at $11\frac{1}{2}\%$.

other significance to, the change in administrative practice as of January 1, 1942, to wit (1) the determination that gross proceeds of sales to the United States, previously thought to be immune from taxation, were to be included in the measure of tax, and (2) the determination that post exchanges and ships' service stores, previously thought to be non-government business enterprises, were to be treated as arms of the federal government engaged in performing governmental functions as integral parts of the War and Navy Departments. Hence the fourth paragraph of appellant's statement of the case (Br. 3-4) has no bearing. Such change of administrative practice in any event is without significance. (Infra, footnote 15.)

Appellant's first claim, that of total exemption, was based on the theory that all sales to the United States were non-taxable (R. 22-23, 102; Ex. B, R. 27-36.) Appellant's second claim, that part of the amount in controversy should be classified as subject to the $\frac{1}{4}$ of 1% rate instead of the $1\frac{1}{2}\%$ rate, was based on an attempted distinction between sales to the post exchanges and ships' service stores of the United States and other federal sales. (R. 22-23, 102; Ex. B, R. 27-36.)

It was stipulated (R. 24) and found (R. 103) that the post exchanges to which appellant sold were substantially similar to those involved in *Standard Oil Co. v. Johnson*, 316 U. S. 481, 62 S. Ct. 1168, 86 L. Ed. 1611. Hence, these post exchanges are "arms of the federal government engaged in performing government functions as integral parts of the War Departments." (R. 106.) It further was stipulated and found that the ships' service stores have the same relation to the United States Navy as the post exchanges have to the United States Army. (R. 25, 103.) Nevertheless, appellant seeks to obtain for his sales to the post exchanges and ships' service stores a rate of tax lower than that admittedly applicable to other sales to the War and Navy Departments, if the claimed exemption is denied. (R. 22-23, 102; Ex. B, R. 27-36.)

The General Excise Tax Law of the Territory imposes a privilege tax against persons on account of their business and other activities in the Territory, measured by values, gross proceeds of sale, or gross income, as the case may be. (Sec. 2, Appendix.) The

tax falls on the business of a manufacturer, a farmer or other producer, a construction contractor, a theatre or other amusement business, services whether professional or otherwise, and every "business, trade, activity, occupation, or calling" not included in a specific provision of the Act. (Sec. 2, Appendix.) Included in the taxes levied by the statute is a tax upon the business of selling tangible personal property in the Territory measured by the gross proceeds of sales of the business. (Sec. 2 B, Appendix.) This tax, consonant with the all inclusive scheme of the statute, falls on every sale, and is not limited to sales at the retail level. The lower court found and decided (R. 98-107, 187, 202) that the tax law divides sales into two classes, viz.:

Class (1). This class includes all sales to the territorial and federal governments and agencies thereof, charitable institutions, hospitals, fraternal benefit societies, public utilities, users and consumers, and others not themselves subject to the tax. This class includes all such sales irrespective of whether the goods are sold in wholesale lots or at wholesale prices, and irrespective of whether the goods are intended to be and are resold by the purchasers, or what is done with such goods. The evidence shows as examples of inclusion in this class irrespective of intended resale, sales to: School cafeterias of the Territory of Hawaii; public utilities selling stoves, refrigerators, heaters and the like but not subject to the general excise tax on such resales because of inclusion thereof in public utility business subject to public utility tax; hospitals and other tax exempt institutions; post exchanges and ships' service

stores. (R. 157-159, 160-163, 164-167.) In all such cases the second sale actually existed but was disregarded (R. 162-163), causing the single taxable sale to be treated as such, whether the reason was that no further sale would occur or that a further sale would not be taxable.

The rate of tax upon this class of sales throughout the period involved was $11\frac{1}{2}\%$.³

Class (2). This class includes only sales to: (a) a licensed retail merchant or jobber for purposes of resale; (b) a licensed manufacturer for incorporation into a product for sale; (c) a licensed contractor for incorporation into the project required by the contract. "Licensed", as used in the act, means and refers to a person subject to the privilege tax imposed by the act and required by the act to take out a license. (R. 106, pars. J and M; R. 198-200.) Hence, this class includes sales of goods which in normal distribution through commercial channels bear two taxes (viz., one when sold at wholesale when the rate is $\frac{1}{4}$ of 1% and one when sold at retail when the rate is $11\frac{1}{2}\%$). This class is distinguished from class (1) sales of goods which do not bear two taxes. The classification is *based upon this difference*, viz., whether double taxation (class 2) or single taxation (class 1) is involved.

The rate of tax upon class (2) sales throughout the period involved was $\frac{1}{4}$ of 1%.

³Wherever the statute (Appendix) mentions $11\frac{1}{4}\%$ the rate of tax during the period in question was $11\frac{1}{2}\%$. The adjustment was made by the Governor pursuant to section 2, subsection III of the tax law. The 1947 tax rate has no bearing on this case.

Throughout the record, for convenience, the $\frac{1}{4}$ of 1% rate has been referred to as "wholesaling" and the $1\frac{1}{2}$ % rate as "retailing." Actually, as the lower court held, application of these rates does not depend upon determination of the common, ordinary sense of those words, the rate of $1\frac{1}{2}$ % being applicable unless appellant's sales meet the statutory requirements for class (2), which are found in section 1, subsection (10) (Appendix) under the statutory definition of "wholesaler." These statutory requirements, in so far as material in this case, are first, that appellant be "a person doing a regularly organized wholesale or jobbing business, known to the trade as such"; this the appellee-tax commissioner concedes that appellant is. Second, that the sales in question be "sales, to a licensed retail merchant or jobber, for purposes of resale"; this requirement the appellant contends was fulfilled; the appellee-tax commissioner contends it was not, and the lower court so held (R. 106, 198-201). Appellant further contends that the requirement that the sales be "to a licensed retail merchant or jobber" is unconstitutional and invalid as applied in this case, though he concedes the validity of the requirement that the sales be "for purposes of resale." Appellee-tax commissioner contends, and the lower court so held, that application of the requirement that the sales be "to a licensed retail merchant or jobber" is valid in this case as in others; moreover, that reading the statute as a whole, the above quoted words are part and parcel of the other admittedly valid requirement that the sales be "for purposes of resale."

QUESTIONS OF LAW INVOLVED.

1. Can the Territory of Hawaii lawfully include in the measure of a privilege tax upon the business of selling tangible personal property in the Territory, the gross proceeds of sales so made to the United States and the post exchanges and ships' service stores which are integral parts thereof?

2. Can the Territory of Hawaii, in a privilege tax act which taxes every sale, service or other activity, avoid the undue pyramiding of the tax by prescribing a lower rate where a second taxable activity is to follow? If it does so, must it segregate and give consideration to an activity of the United States which, for taxation purposes, it is required to disregard?

STATUTES INVOLVED.

The General Excise Tax Law, as amended to and including the 1943 legislative session, is reproduced in the Appendix.

The period involved in this case is October 1, 1942 to and including March 31, 1944. Hence, the amendments made in 1943 were not in effect during the whole period; these 1943 amendments are set out in the Appendix in italics.

SUMMARY OF ARGUMENT.

(The below designation of points corresponds to that used in appellant's brief, pp. 15-16.)

A. The Territory of Hawaii lawfully can include in the measure of a privilege tax upon the business of selling tangible personal property in the Territory, the gross proceeds of sales made to the United States, its post exchanges and ships' service stores.

1 and 2. The Territory of Hawaii was created by Congress as a sovereign government with full power to impose taxes. The Territory's power to tax the United States and its instrumentalities is as great as, and no greater than, the powers of the states with respect to such taxation.

3 and 4. The inclusion of gross proceeds of sales to the United States, its post exchanges and ships' service stores, in the measure of a privilege tax upon the business of selling tangible personal property in the Territory, has only an economic effect upon the federal government, and does not constitute the tax an invalid burden upon or interference with federal activities. The *Panhandle* line of cases has been overruled.

B. The Territory of Hawaii lawfully can tax the gross proceeds of sales to post exchanges and ships' service stores at $11\frac{1}{2}\%$, the same as other sales to the federal and territorial governments, exempt institutions, and consumers.

1. The Supreme Court of Hawaii has interpreted the statute as classifying sales to post exchanges and ships' service stores with sales to the federal and territorial governments and others, where no second taxable activity occurs.

Such is not “manifest error”; indeed it is obviously correct.

2. The legislative classification was made to avoid undue pyramiding of the general excise tax; it consistently carries out this purpose without discrimination and is constitutional.

ARGUMENT.

A. THE TERRITORY OF HAWAII LAWFULLY CAN INCLUDE IN THE MEASURE OF A PRIVILEGE TAX UPON THE BUSINESS OF SELLING TANGIBLE PERSONAL PROPERTY IN THE TERRITORY, THE GROSS PROCEEDS OF SALES MADE TO THE UNITED STATES, ITS POST EXCHANGES AND SHIPS' SERVICE STORES.

1 and 2. The Territory of Hawaii was created by Congress as a sovereign government with full power to impose taxes. The Territory's power to tax the United States and its instrumentalities is as great as, and no greater than, the powers of the States with respect to such taxation.

That the Territory of Hawaii was created by Congress as a sovereign government was held in *Kawananakoa v. Polyblank*, 205 U.S. 349, 27 S. Ct. 526, 51 L. Ed. 834. Both this court and other courts having appellate jurisdiction over territories repeatedly have supported the taxing power of the territories. It is “the full taxing power” which Congress itself could have exercised. *Yerian v. Territory of Hawaii*, 130 F. 2d 786, 788 (C.C.A. 9th 1942) and cases cited; *Rivera v. Buscaglia*, 146 F. 2d 461 (C.C.A. 1st 1944); *Haavik v. Alaska Packers Assn.*, 263 U.S. 510, 513.

With respect to claims of federal immunity, this court has held that the rules governing the power to tax are the same as govern the states, and that the overruling of the doctrine of the tax immunity of those dealing with the federal government is as effective in the Territory of Hawaii as elsewhere. “* * * the power conferred by #55 [of the Hawaiian Organic Act] is as great as, and no greater than, the powers of the States with respect to such taxation.” *Yerian v. Territory*, supra, and cases cited.⁴

There remains to be considered the contention that “the power that is given them [the territories] by Congress depends upon what Congress thought it was granting at the time of the enactment of the power granting act.” (Br. pp. 22-23.) The answer above made is: Congress thought it was granting the Territory of Hawaii the same power as a state. *Yerian v. Territory*, supra. Because Congress so intended the distinction made elsewhere in appellant’s brief (Br. 39-42) between states and territories based on the duality of sovereignty where the states and the federal government are concerned, is of no materiality. Indeed, the Supreme Court of the United States has suggested that the duality of sovereignty requires

⁴130 F.2d 786, 789. To the same effect as the *Yerian* case and cases there cited, are *Rivera v. Buscaglia*, supra; *Gromer v. Standard Dredging Co.*, 224 U.S. 362, 371, 32 S.Ct. 499, 56 L.Ed. 801. While it is not to be presumed that Congress intends a territory to possess more taxing power than a state, a territory by specific authority of Congress may even possess taxing power denied to a state. *Inter-Island Co. v. Hawaii*, 305 U.S. 306, 59 S.Ct. 202, 83 L.Ed. 189; *Buscaglia v. Ballester Hermanos*, 162 F.2d 805 (C.C.A. 1st 1947), cert. den. U.S., S.Ct., 92 L.Ed.Adv.Sh. 78.

greater *judicial* protection of the federal government against state taxation than in the case of territorial taxation where *congressional* protection can be invoked. *Talbott v. Silver Bow County*, 139 U.S. 438, 445-446, 11 S. Ct. 594, 35 L. Ed. 210.

The citation in appellant's brief (Br. pp. 23-25, 27) of certain cases in which statutes have been interpreted in their historical setting, implies a further contention, not directly made, that the judicial decisions of 1900, the date of enactment of the Hawaiian Organic Act, should be read into that Act.

In the first place, the contention is one which if meritorious would have led to a different result in the *Yerian* case. That case involved a tax on a federal salary, which prior to 1900 had been held to fall under the blanket of federal immunity.⁵ The earlier cases were overruled by *Graves v. People of New York ex rel O'Keefe*,⁶ and this court perceived no necessity that the Hawaii Organic Act be amended, in order to give that case effect.

In the second place, the contention now under consideration, actually present but not specifically argued in the *Yerian* case, was fully presented and summarily denied in a similar case arising in Puerto Rico in which the taxpayer sought to freeze into the Organic Act the doctrine of *Collector v. Day*.⁷ This similar case is *Rivera v. Buscaglia*, *supra*.⁸

⁵*Dobbins v. Commissioners*, 16 Pet. 435, 10 L.Ed. 1022 (1842); *Collector v. Day*, 11 Wall. 113, 20 L.Ed. 122 (1870).

⁶306 U.S. 466, 59 S.Ct. 595, 83 L.Ed. 927.

⁷*Supra*, footnote 5.

⁸146 F.2d 461, 462 (C.C.A. 1st 1944).

In the third place, the contention is one which in this case arrives nowhere. Appellant relies on the *Panhandle* line of cases (Br. 17-18, notes 4-6), which originated in 1928, and which the Supreme Court commenced to "limit" in 1937,⁹ and finally overruled in 1941.¹⁰ At the time of the Hawaiian Organic Act *Tabott v. Board of Commissioners of Silver Bow County*, supra,¹¹ was the law, holding that the presumed intent of Congress is to confer on the territories as great a taxing power with respect to federal instrumentalities as the states'.

In the fourth place, the general rule is that a grant of taxing power is presumed to be complete, and to carry with it without further enactment, all enlargements thereof by judicial decision or congressional legislation. *Philadelphia v. Schaller*, 148 Pa. Super. 276, 25 A. 2d 406, cert. den. 317 U.S. 649, 63 S. Ct. 43, 87 L. Ed. 522 (1942); *Kiker v. Philadelphia*, 346 Pa. 624, 31 A. 2d 289, cert. den. 320 U.S. 741, 64 S. Ct. 41, 88 L. Ed. 439; *Boeing Aircraft Co. v. R. F. C.*, 25 Wash. 2d 652, 171 P. 2d 838 (1946). Construing an act of Congress which could have required immunity from state taxation but did not do so, enacted at a time when such tax immunity existed by judicial decision, the Supreme Court of the United States said:

⁹*James v. Dravo Contracting Co.*, 302 U.S. 134, 151, 58 S.Ct. 208, 217, 82 L.Ed. 155, 168.

¹⁰*Alabama v. King & Boozer*, 314 U.S. 1, 62 S.Ct. 43, 86 L.Ed. 3; *Curry v. United States*, 314 U.S. 14, 62 S.Ct. 48, 86 L.Ed. 9.

¹¹139 U.S. 438, 11 S.Ct. 594, 35 L.Ed. 210 (1891).

“The immunity formerly said to rest on constitutional implication cannot now be resurrected in the form of statutory implication.”

Oklahoma Tax Commission v. United States,
319 U.S. 598, 604, 63 S. Ct. 1284, 1286, 87
L. Ed. 1612, 1617 (1943).

In the fifth place, the cases cited in appellant's brief turn on a particular legislative history showing a specific intent to freeze into the statute in question the prevailing law. These cases have been so distinguished.¹²

In the sixth place, the tax here involved, unlike the tax in *Helvering v. Griffiths*¹³ cited by appellant (Br. 27-28), concerns the period *after* the new constitutional doctrine was inaugurated. That taxpayers should be entitled to rely on constitutional law cases as they stand at the time of the accrual of the tax is a proposition not controverted by the actions of the tax commissioner in this case.

Appellant's brief makes passing mention of the fact that the Territory did not attempt to tax the proceeds of sales to the United States until January 1, 1942 (Br. 21-22). In the lower court this was urged as having bearing on the construction of section 3 of the general excise tax law, but the assignments of error which would raise this point have been aban-

¹²*United States v. South-Eastern Underwriters' Association*, 322 U.S. 533, 556-8, 64 S.Ct. 1162, 1175-76, 88 L.Ed. 1440, 1459-60;

Commissioner v. Shumberg Estate, 144 F.2d 998, 1003 (C.C.A. 2d 1944), cert. den. 323 U.S. 792, 65 S.Ct. 433, 89 L.Ed. 631.

¹³318 U.S. 371, 63 S.Ct. 636, 87 L.Ed. 843,

doned.¹⁴ If appellant's brief intends to suggest that a new legislative enactment by the tax levying authority is necessary to take advantage of the narrowing of federal immunity (whether by judicial decision or congressional legislation), the point clearly is erroneous.¹⁵

3 and 4. The inclusion of gross proceeds of sales to the United States, its post exchanges and ships' service stores, in the measure of a privilege tax upon the business of selling tangible personal property in the Territory, has only an economic effect upon the Federal Government, and does not constitute the tax an invalid burden upon or interference with Federal activities. The Panhandle line of cases has been overruled.

Appellant's brief takes the position that the *Panhandle* line of cases has not been overruled (Br. pp. 28-39). This issue no longer is an open one. In *Alabama v. King and Boozer*, supra,¹⁶ the Supreme Court said that the federal immunity doctrine:

"* * * does not spell immunity from paying the added costs, attributable to the taxation of those who furnish supplies to the Government and who have been granted no tax immunity. So far as

¹⁴Those assignments were 3, 4, and 2.

¹⁵*Cook v. Wilson*, 83 Ark. 938, 187 S.W.2d 7 (1945), aff'd sub. nom. *Wilson v. Cook*, 327 U.S. 474, 66 S.Ct. 663, 90 L.Ed. 793;

Western Lithograph Co. v. State Board of Equalization, 11 Cal.2d 156, 78 P.2d 731 (1938);

Compress of Union v. Stone, 188 Miss. 49, 193 So. 329 (1940), cert. den. 311 U.S. 668, 61 S.Ct. 27, 85 L.Ed. 429;

Great Atlantic & Pacific Tea Co. v. City of Richmond, 183 Va. 931, 33 S.E.2d 795 (1945);

Duhamel v. State Tax Commission, Ariz., 179 P.2d 252 (1947).

¹⁶314 U.S. 1, 62 S.Ct. 43, 86 L.Ed. 3.

a different view has prevailed, see *Panhandle Oil Co. v. Knox*, supra; *Graves v. Texas Co.*, supra, we think it no longer tenable.”

p. 9.

The headnote of this case reads:

“(1) The fact that the economic burden of the tax is passed on to the United States does not make it a tax upon the United States. *Panhandle Oil Co. v. Knox*, 277 U.S. 218, and *Graves v. Texas Co.*, 298 U.S. 393, overruled. p. 9.”

p. 1.

In the later case of *Penn Dairies v. Milk Control Commission*, 318 U.S. 261, 63 S. Ct. 617, 87 L. Ed. 748 (1943) the Supreme Court itself said that it had overruled the *Panhandle* line of cases in the *King and Boozer* case. The court said of certain early opinions of the Comptroller General:

“* * * All rest on the reasoning of *Panhandle Oil Co. v. Knox*, 277 U.S. 218, and like cases, which were overruled in *Alabama v. King & Boozer*, supra. * * *”

p. 277.

The trial court held (R. 104-105) following the previous opinion of the Supreme Court of Hawaii (R. 193-195), and the Supreme Court affirmed the trial court (R. 187), that the tax in question is a tax upon the business of selling tangible personal property in the Territory, measured by the gross proceeds of sales of the business, including all sales made to the United States government, its departments and agencies; that the tax so imposed is a tax upon the

plaintiff-appellant and does not levy a burden upon or interfere with federal activities; and that such tax has only an indirect economic effect upon the United States government, its departments, and agencies.

That the tax act is of the nature so set forth is clear from its provisions (Appendix). Nowhere in the tax act is the vendor required to collect the tax from the purchaser, or the purchaser made liable therefor. The question before this court is the duty of Thomas H. Brodhead, doing business as T. H. Brodhead Co., to pay the tax.¹⁷

It is noteworthy¹⁸ that the United States, to whom the tax immunity is supposed by appellant to belong, does not claim it. The obvious reason for the non-appearance of the United States in this proceeding is that the Attorney General advised the War Department to "take no part in any effort to prevent the collection of the tax¹⁹ from dealers domiciled in the Territory [of Hawaii] on sales made by them to such post exchanges". 39 Ops. Atty. Gen. 316 (1939). And the Comptroller General has disclaimed interest in the collection of a tax of the type here involved from a vendor selling supplies to the United States, saying:

"* * * the language used by the Supreme Court of the United States in its decision in the case of

¹⁷Compare *Federal Land Bank v. Bismarck Co.*, 314 U.S. 95, 62 S.Ct. 1, 86 L.Ed. 65, where the question before the court was the duty of the federal instrumentality-purchaser to pay a tax construed by the state court as a sales tax laid upon the purchaser.

¹⁸*James v. Dravo Contracting Co.*, supra, 302 U.S. 134, 158, 58 S.Ct. 208, 82 L.Ed. 155.

¹⁹The tax there involved was the Hawaiian Tobacco Tax, imposed by Act 220 of the Session Laws of Hawaii 1939.

Alabama v. King & Boozer, 314 U.S. 1, leaves no room for doubt that a person who sells supplies to the United States is not—merely because of the immunity of the Federal Government from State taxation—exempt from the payment of an otherwise applicable State tax where it appears that the legal incidence of the tax rests upon him as the vendor and not upon the United States as the vendee. * * *.”

24 Comp. Gen. Dec. 150, 152.²⁰

The interest sometimes taken by the United States in the collection of a tax on sales to it has been coupled with the admission that the tax was valid if imposed on the vendor, the United States being concerned only if, under the particular tax law, the legal incidence of the tax fell on the purchaser. *United States v. Lee*, 153 Fla. 94, 13 S. 2d 919 (1943).²¹

This distinction between a tax such as the general excise tax here involved, and a true sales tax required to be added to the price and collected from the vendee *qua* tax, has been deemed important by law writers on the subject. Thus, as late as July 1945 Professor Powell, while having no doubt that the *Panhandle* line of cases had been overruled as to a tax of the first type imposed solely on the vendor,²² thought

²⁰The Comptroller General had rendered a similar opinion as early as 1938. 17 Comp.Gen.Dec. 863.

²¹In this case the United States was represented by *Samuel O. Clark, Jr.*, then the head of the tax division of the Department of Justice.

²²At page 789 of 58 Harv.L.R. Professor Powell says: “The new light now is that the United States should pay its way if it pays it merely through increase of charges by contractors *and vendors* or through possible higher salaries.” (*Italics added.*)

that this line of cases had not yet been overruled as to a tax of the latter type, when applied to a sale to the United States.²³

Even this remaining doubt has been put at rest. In *Wilson v. Cook*, 327 U.S. 474, 66 S. Ct. 663, 90 L. Ed. 793 (1946),²⁴ there was involved an Arkansas statute which imposed "a privilege or license tax * * * upon each person * * * engaged in the business of * * * severing from the soil * * * for commercial purposes natural resources, including * * * timber * * *". The tax was at the rate of seven cents per thousand feet of timber severed. The taxpayer was required to "collect or withhold out of the proceeds²⁵ of the sale of the products severed the proportionate parts of the total tax due by the respective owners of such natural resources at the time of severance".

The United States, as owner of timberland, made a contract with Wilson Lumber Company for the purchase and severance of timber on national forest reserves. Title to the timber was to remain in the United States until it was paid for.

Wilson Lumber Company having been assessed for the tax, sued to enjoin its collection. The Supreme Court of Arkansas held that the tax assessed against Wilson Company did not lay an unconstitutional

²³"*The Waning of Intergovernmental Tax Immunities*", 58 Harv.L.R. 633, 657; "*The Remnant of Intergovernmental Tax Immunities*", 58 Harv.L.R. 757, 763.

²⁴This case was decided on the very day that the Supreme Court of Hawaii rendered its opinion (R. 191).

²⁵Italics added.

burden on the United States. The Supreme Court of the United States granted certiorari.

Wilson Company contended among other points that "the tax is unconstitutional as a tax laid upon the property or activities of the United States, or because the tax laid on plaintiffs [Wilson Lumber Company] imposed an unconstitutional burden on the United States".

The contention that the mere laying of the tax on Wilson Lumber Company measured by the amount of timber purchased by it from the United States constituted an unconstitutional burden on the United States, was summarily denied, the court saying:

"Our decision in *James v. Dravo Contracting Co.*, *supra*, and in *Alabama v. King & Boozer*, *supra*, and the cases cited in those opinions, can leave no doubt that the Supreme Court of Arkansas correctly held that plaintiffs, who are taxed by the state on their activities in severing lumber from Government lands under contract with the Government, cannot claim the benefits of the implied constitutional immunity of the Federal Government from taxation by the state."

pp. 482-483.

Thus, with respect to the type of tax here involved, imposed on one dealing with the United States for the privilege of so doing, the validity thereof is beyond doubt; it is characterized by the Supreme Court of the United States as having been placed beyond doubt by the decisions in the *Dravo Contracting Company* and *King and Boozer* cases.

There was involved in the *Wilson* case the further question of the effect of the requirement, not present in the Hawaii statute, that the tax be passed on to the United States; the severer of the timber was required to withhold the tax from the proceeds of the sale of the products severed. This type of tax, as above noted, was the only type of tax theretofore resisted by the United States, and it filed a brief as amicus curiae in this case. It was contended that by reason of this feature of the law it placed "a forbidden tax directly on the United States" and comparison was made with *Mayo v. United States*, 319 U.S. 441, 63 S. Ct. 1137, 87 L. Ed. 1504.

The Supreme Court confined its decision to the case before it as framed in the state court, that is, the collectibility of the tax from Wilson Company; the court did not decide whether or not that company could collect the tax from the United States. It was too late to raise that question, the court said.

Considering the effect of the collection provision on Wilson Company, the court held that this feature of the law did not bring Wilson Company within the protection of the federal immunity doctrine. The line of division between a tax on one dealing with the United States and a tax on the United States could not be made clearer than it is made in this case. Said the court,

"We obviously do not by our judgment against the plaintiffs [Wilson Company] impose the tax on the Government."

pp. 484-485.

Upon comparison of the dissenting opinion of Mr. Rutledge with the majority opinion, an even greater significance of the decision appears. This will be developed in Part B of this brief.

By reason of the number and decisive character of the authorities involving dealings with the United States, resort to cases involving interstate and foreign commerce is uncalled for. We therefore have refrained from analyzing the cases in this field cited by appellant²⁶ or adding others of that nature.

The authorities upon which appellee-tax commissioner relies, all involving dealings with the United States, are presented in chronological order commencing with the *Dravo Contracting Company* case, as follows:

James v. Dravo Contracting Co., supra, 302 U.S. 134, 149, 58 S. Ct. 208, 82 L. Ed. 155 (1937). A privilege tax on a contractor having a lump sum contract with the United States, measured by the gross proceeds of his contract, is valid.

Western Lithograph Co. v. State Bd. of Equalization, supra, 11 Cal. 2d 156, 78 P. 2d 731 (1938). A sales tax on a vendor to a national bank, measured by the gross proceeds of sale, and authorized but not required to be separately stated in the charge to the vendee, is valid.

²⁶(Br. 37-38.) The General Excise Tax Law of the Territory of Hawaii definitely was not modeled after the Indiana Gross Income Tax Law as claimed in appellant's brief (Br. 37). It is of the type exemplified by the West Virginia Law (West Va. Code of 1943, c. 11, art. 13).

Federal Land Bank v. De Rochford, 69 N. D. 382, 287 N. W. 522 (1939). A tax on a sale of motor vehicle fuel to a federal land bank is valid.

Compress of Union v. Stone, *supra*, 188 Miss. 49, 193 So. 329 (1940). A gross income tax applied to receipts from compressing of cotton for Commodity Credit Corporation, a wholly owned federal instrumentality, is valid.

Alabama v. King & Boozer, *supra*, 314 U. S. 1, 62 S. Ct. 43, 86 L. Ed. 3 (1941). A sales tax the incidence of which is on the vendee, to whom it is passed on, imposed on a federal cost-plus contractor purchasing lumber for delivery to the construction site where, according to the government contract, title passes to the United States and the United States becomes obligated to reimburse the contractor, is valid.

Curry v. United States, *supra*, 314 U. S. 14, 62 S. Ct. 48, 86 L. Ed. 9 (1941). A use tax imposed on a federal cost-plus contractor importing roofing from without the state, on account of his use of the roofing in the performance of a federal contract under an agreement for reimbursement by the United States, is valid.

Federal Land Bank v. Bismarck Co., *supra*, 314 U.S. 95, 62 S. Ct. 1, 86 L. Ed. 65 (1941). A sales tax the incidence of which is on the vendee, to whom it is required to be passed on, when imposed on a purchase by a federal land bank cannot be collected from that bank.

Penn Dairies v. Milk Control Commission, supra, 318 U.S. 261, 63 S. Ct. 617, 87 L. Ed. 748 (March, 1943). A requirement that a vendor of milk shall charge a minimum price therefor, is valid as applied to the sale of milk to the United States.

United States v. Lee, supra, 153 Fla. 94, 13 S. 2d 919 (June 1943). A tax on the privilege of selling gasoline the incidence of which is on the vendor, applied to a sale to the United States, is valid.

Mayo v. United States,²⁷ supra, 319 U. S. 441, 63 S. Ct. 1137, 87 L. Ed. 1504 (June 1943). (Br. 35.) An inspection fee imposed on importations of commercial fertilizer into Florida cannot be exacted for commercial fertilizer owned by the United States and brought into Florida by it for distribution under the Soil Conservation and Domestic Allotment Act.

*United States v. Allegheny County*²⁸ (*Mesta Machine Co.* case), 322 U. S. 174, 64 S. Ct. 908, 88 L. Ed. 1209 (1944). (Br. 36, 38.) An *ad valorem* property tax assessed upon the land and plant of Mesta Machine Company, including in the measure of the tax the value of equipment owned by the United States without limitation to the value of the company's own interest therein as the lessee of the United States, is invalid.

Smith v. Davis, 323 U. S. 111, 65 S. Ct. 157, 89 L. Ed. 107 (1944). An *ad valorem* tax on an open ac-

²⁷This case will be further considered in Part B of this brief.

²⁸This case will be further considered in Part B of this brief.

count receivable for money due from the United States, arising out of a construction contract is valid.

Carnegie-Illinois Steel Corp. v. Alderson, 127 W. Va. 807, 34 S. E. 2d 737 (1945), cert. den. 326 U. S. 764, 66 S. Ct. 146, 90 L. Ed. 460. A steel company occupying, as lessee, an ordinance plant owned by the United States, under an agreement requiring it to sell the entire output to the United States at fixed prices, is liable for the West Virginia tax on the privilege of manufacturing, measured by the gross proceeds of sale of the product to the United States.

Wilson v. Cook,²⁹ supra, 327 U. S. 474, 66 S. Ct. 663, 90 L. Ed. 793 (1946). A company purchasing and severing timber from United States owned land is liable for a tax on the privilege of engaging in such business, measured by the volume of timber cut.

S.R.A., Inc. v. Minnesota,³⁰ 327 U. S. 558, 66 S. Ct. 749, 90 L. Ed. 851 (1946). An abandoned post office site sold by the United States as surplus real estate under a contract entitling the purchaser to possession but retaining legal title in the United States for security purposes, may be assessed to the purchaser at its full value even though he still owes a substantial part of the purchase price, where the assessment is made subject to the fee title of the United States and no lien is claimed on the United States title.

²⁹This case will be further considered in Part B of this brief.

³⁰This case will be further considered in Part B of this brief.

R.F.C. v. Beaver County, 328 U. S. 204, 66 S. Ct. 992, 90 L. Ed. 1172 (1946). In consenting to taxation of "real property" of the United States, Congress intended that there might be included therein whatever by state law was deemed real property, e.g., machinery included by Pennsylvania in the assessment of a manufactory.

Sanders v. Oklahoma Tax Commission, 197 Okla. 285, 169 P. 2d 748 (1946), cert. den. 329 U. S. 780, 67 S. Ct. 202, 91 L. Ed. Adv. Sh. 80. A federal contractor using gasoline in tractors and other machinery for the performance of his construction contract with the United States, is liable to a state tax upon such use notwithstanding the fact that by reason of the state's cession of exclusive jurisdiction of the federal area where the use occurs, the state is dependent upon congressional authorization for the tax, and Congress has only consented "when such fuels are not for the exclusive use of the United States".

Kaiser Co. v. Reid,³¹ 30 Cal. Adv. 614, 184 P. 2d 879 (1947). A nontransferable exclusive use of shipyards and facilities owned by the United States is a possessory interest taxable to the occupant upon the value of the possessory interest, even though it is operating the yard as a cost-plus contractor, its agreement will require the United States to pay the tax, and the United States intervenes in the case to protest the tax.

³¹This case will be further considered in Part B of this brief.

Jefferson County v. United States, 164 F. 2d 184 (C.C.A. 5th, 1947). Land bought by the United States with funds transferred to it by the Florida Rural Rehabilitation Corporation and subsequently resold to individual purchasers is not subject to tax prior to the sale, irrespective of the use made of the land.

Salt Lake County v. Kennecott Copper Corp., 163 F. 2d 484 (C.C.A. 10th, 1947), cert. den. U. S., S. Ct., 92 L. Ed. Adv. Op. 400, Feb. 9, 1948. Where a Utah statute, as interpreted by the Utah Supreme Court, which interpretation is followed, requires that mines (in addition to the improvements and machinery thereof) be assessed at \$5 per acre plus twice the gross proceeds realized during the preceding calendar year from the sale or conversion of ores into money (called the "net annual proceeds"), and that there be included in these proceeds a subsidy paid by the United States per pound for minerals produced in excess of fixed quotas, inclusion of the subsidy does not invalidate the tax.

- B. THE TERRITORY OF HAWAII LAWFULLY CAN TAX THE GROSS PROCEEDS OF SALES TO POST EXCHANGES AND SHIPS' SERVICE STORES AT 1½%, THE SAME AS OTHER SALES TO THE FEDERAL AND TERRITORIAL GOVERNMENTS, EXEMPT INSTITUTIONS, AND CONSUMERS.**
1. The Supreme Court of Hawaii has interpreted the statute as classifying sales to post exchanges and ships' service stores with sales to the Federal and Territorial Governments and others, where no second taxable activity occurs. Such is not "manifest error"; indeed it is obviously correct.

This point involves the interpretation of the tax act. Counsel for appellant concedes the well settled rule that the construction of a statute by the Supreme Court of Hawaii is to be accepted by this Court unless manifestly erroneous (Br. 45).³²

Appellant's difference with the Supreme Court of Hawaii in the matter of interpretation carries over into appellant's argument as to the validity of the rate provisions. That is to say, appellant having set up the classification of taxpayers as he sees it persists in using this same classification in point 2 of part B of his brief, where discrimination is asserted. Obviously, to apply the interpretation of the Supreme Court of Hawaii, we must apply not only the tax rate it found due, but the classification it made for rate purposes, and the legislative intent found to call

³²Citing *Waiialua Agricultural Co. v. Christian*, 305 U.S. 91, 59 S.Ct. 21, 83 L.Ed. 60, reh'g den. 305 U.S. 673, 59 S.Ct. 240, 83 L.Ed. 436. Cases in this court involving the interpretation of tax statutes and so holding, are *Hawaii Consolidated Ry v. Borthwick*, 105 F.2d 286 (1939); *Lord v. Territory*, 79 F.2d 761 (1935); *Hill v. Carter*, 47 F.2d 869 (1931); *Honolulu Rapid Transit v. Wilder*, 36 F.2d 159 (1929); *Ewa Plantation Co. v. Wilder*, 289 Fed. 664, 670 (1923), and cases cited.

for this classification. The only question then remaining is whether *this classification* is valid.

Shortly stated, the Supreme Court of Hawaii found that post exchanges and ships' service stores belong in the same class as the War and Navy Departments of which they are integral parts, and in which they function as arms of the federal government performing federal functions. Appellant persists in classing post exchanges and ships' service stores as "retail merchants", and even if this court should hold that they are not such within the meaning of the tax act, he still argues that sales to them must receive the same treatment as sales to retail merchants.

As set forth in the "statement of the case" supra, the General Excise Tax of the Territory falls on the business of a manufacturer, a farmer or other producer, a construction contractor, a theatre or other amusement business, services whether professional or otherwise, and every "business, trade, activity, occupation, or calling" not included in a specific provision of the Act. (Sec. 2, Appendix.) Included in the taxes levied by the statute is a tax upon the business of selling tangible personal property in the Territory measured by the gross proceeds of sales of the business. (Sec. 2B, Appendix.) This tax, consonant with the all inclusive scheme of the statute, falls on every sale, and is not limited to sales at the retail level. At the time in question the rate of tax on each and every activity was fixed at $1\frac{1}{2}\%$,³³ with only two

³³This was in lieu of the $1\frac{1}{4}\%$ specified in the statute, by virtue of an adjustment made under subsection III of section 2.

exceptions: (1) Manufacturers of products other than sugar, pineapples and other canned goods, were taxed at $\frac{1}{4}$ of 1%. (2) Persons engaged in the business of selling tangible personal property in the Territory were taxed at $\frac{1}{4}$ of 1% if they could qualify as wholesalers or producers, otherwise at $1\frac{1}{2}\%$.

Appellant rests his claim to the reduced rate on the contention that he qualifies as a "wholesaler". It must be noted here that the burden of sustaining this claim is on the appellant. Appellee-tax commissioner has shown that appellant is a "person engaging or continuing within this Territory in the business of selling any tangible personal property whatsoever" and that he had certain "gross proceeds of sales of the business" (quoting from Sec. 2B, Appendix). That is enough to cause the tax to apply at the rate of $1\frac{1}{2}\%$ unless appellant becomes entitled to a deduction by bringing himself within the "wholesaler" provisions. He claims a favored position, which like an exemption provision is a privilege, and like an exemption provision must be strictly construed.³⁴

To qualify as a wholesaler appellant must meet the definition set forth in section 1, subsection (10), of the statute (Appendix), particularly clause (a) thereof upon which he bases his claim. The relevant provision reads as follows:

³⁴¹ *Merten's Law of Federal Income Taxation*, Sec. 3.08;
Remco S. S. Co. v. Commissioner, 82 F.2d 988 (C.C.A. 9th),
 cert. den. 299 U.S. 555, 57 S.Ct. 17, 81 L.Ed. 409;
Bank of Hawaii v. Wilder, 8 F.2d 845 (C.C.A. 9th);
Atlantic Coast Line R. Co. v. Phillips, 332 U.S. 168, 67 S.Ct.
 1584, 91 L.Ed.Adv.Sh. 1538 (1947);
Re Excise Tax Robert Hind, Ltd., 34 Haw. 40,

“(10) ‘Wholesaler’ or ‘jobber’ shall ‘apply only to a person doing a regularly organized wholesale or jobbing business, known to the trade as such, and only with respect to the following sales: (a) sales, to a licensed retail merchant or jobber, for purposes of resale; * * *’”³⁵

It is conceded that appellant’s business is known to the trade as a wholesale business. The ground of disallowance of the claimed classification was failure to meet the requirements of clause (a).

Appellant urges that it was “manifest error” for the Supreme Court of Hawaii not to adopt the opinion of the dissenting judge.³⁶ Clause (a) was interpreted by the dissenting judge (R. 218, 235) as having exactly the same meaning as if it read “sales for purposes of resale”, omitting the key words “to a licensed retail merchant or jobber”. According to the dissenting judge every entity which resells is either a retail merchant or jobber (R. 218-219); and every reseller is “licensed”, for it either is lawfully authorized to resell without the license required by section 21 (Appendix) and hence “licensed” by the authority that permits this (R. 235) or is licensed

³⁵The alternative definition of “wholesaler”, to be used in the event the consumption tax law of the Territory should be invalidated by judicial decision (Sec. 1(10), Appendix), has not come into effect (Cf. Br. 46, where the alternative definition is quoted but the statutory explanation as to the use of the alternative definition is omitted).

³⁶The dissenting judge differed from the majority only as to the points involved in Part B of this brief.

under section 21 itself in the sense in which the majority (R. 199-200) used the term.³⁷

By this method the words "to a licensed retail merchant or jobber" were read by the dissenting judge the same as the words "for purposes of resale" already in the statute, and the additional limitation required by the words "to a licensed retail merchant or jobber" was deleted by him from the statute. Such judicial deletion of statutory language of course is not permissible,³⁸ and is manifest error.

The majority opinion gave full effect to the language used by the legislature. It interpreted "retail merchant" as referring to one engaged in business as distinguished from the performance of governmental functions³⁹ (R. 200-201), and "licensed" as

³⁷The dissenting judge deliberately widened the wholesaler class, in order to narrow the class taxable at 1½% from "every person" not a wholesaler or producer, to "every retailer" (R. 216). This was under the mistaken assumption that the running head of subsection B of section 2 was controlling. Of course, such a heading is not controlling, nor can it be used to create an ambiguity where none exists. 2 *Sutherland, Statutory Construction*, 3d ed., secs. 4903, 4802; majority opinion, R. 197-8, 201-2. Even if the heading had the importance assigned to it by the dissenting judge it would merely narrow those taxed under subsection B to "retailers", "wholesalers", and "producers", each of which is defined in section 1. There would be no occasion to widen the class of "wholesaler" any more than that of "retailer", and those sales not falling under either definition would be taxable under subsection H of section 2 at 1½%.

³⁸It violates the cardinal rule of statutory construction that courts are bound to give effect to all parts of a statute; "no sentence, clause or word shall be construed as unmeaning or surplusage if a construction can be legitimately found which will give force to and preserve all the words of the statute". *In re Pringle*, 22 Haw. 557, 564.

³⁹This interpretation is supported by a decision in a similar case, *State v. Owin*, 191 La. 617, 186 So. 46 (1938). There the statute

referring to those required by section 21 of the act to take out a license and themselves pay a tax (R. 199-200). As a result all sales, as well as other activities, are taxed at $1\frac{1}{2}\%$, except those sales which in normal distribution through commercial channels bear two taxes (viz., one when sold at wholesale and one when sold at retail). Only as to those sales is the reduced rate of $\frac{1}{4}$ of 1% allowed, in order to avoid undue pyramiding of the tax. This leaves /subject to the $1\frac{1}{2}\%$ tax all cases where only single taxation is involved, designated by the trial court as class (1) sales (R. 105-106), and including all sales to the territorial and federal governments and agencies thereof, charitable institutions, hospitals, fraternal benefit societies, public utilities, users and consumers, and others not themselves subject to the tax. This class includes all such sales irrespective of whether the goods are sold in wholesale lots or at wholesale prices, and irrespective of whether the goods are intended to be and are resold by the purchasers, or what is done with such goods. The evidence shows as examples of inclusion in this class irrespective of intended resale, sales to: School cafeterias of the Territory of Hawaii; public utilities selling stoves, refrigerators, heaters and the like but not subject to

imposed a license tax, the tax on retail dealers being at a higher rate than the tax on wholesale dealers. In order to be classed as a wholesale dealer the taxpayer had to show that he sold to "dealers for resale". His business was that of buying gold and silver, which he melted, made into bars or plates, and then sold. Ninety per cent of the gold and silver handled by him was sold to the United States. The court held "that the United States Government cannot be classified as a dealer in old gold and silver", and that the taxpayer must pay at the retail rate.

the general excise tax on such resales because of inclusion thereof in public utility business subject to public utility tax; hospitals and other tax exempt institutions; post exchanges and ships' service stores. (R. 157-159, 160-163, 164-167.) In all such cases the second sale actually existed but was disregarded (R. 162-163), causing a single taxable sale to be treated as such, whether the reason was that no further sale would occur or that a further sale would not be taxable.

So read the statute is one which makes a classification based upon the purpose of avoiding undue pyramiding of the tax or double taxation.⁴⁰ The scope of the tax act is all inclusive, and with few exceptions the rate of tax on each activity is 1½%. If it were not for the provision in question it frequently would happen that the distribution of an item of goods carried two or more taxes at 1½%.

There remains to be considered the validity of the classification so made; this is the subject of point 2 of this part, in which the correctness of the Supreme Court of Hawaii's interpretation will be further considered.

⁴⁰That this was the "reason and spirit" of the provision for the lower tax rate was considered by the majority (R. 202). The "reason and spirit" of the law is stated by the legislature to be "one of the most effectual means of discovering the true meaning of the law". (Sec. 12, Revised Laws of Hawaii 1945.) The dissenting judge did not take into account the purpose of the statute. His opinion states that the legislature intended to prevent the lower tax rate from applying in the case of a wholesaler selling to a consumer (R. 219) but does not state what purpose was served thereby that would not also be served by the provision as construed by the majority.

2. The legislative classification was made to avoid undue pyramiding of the General Excise Tax; it consistently carries out this purpose without discrimination and is constitutional.

In this part of the brief appellee-tax commissioner submits argument on the questions stated earlier in this brief, to wit:

Can the Territory of Hawaii, in a privilege tax act which taxes every sale, service or other activity, avoid the undue pyramiding of the tax by prescribing a lower rate where a second taxable activity is to follow? If it does so, must it segregate and give consideration to an activity of the United States which, for taxation purposes, it is required to disregard?

The answers to these questions clearly support the tax statute. But it should be noted that the appellee-tax commissioner does not have the burden of supporting it. It is for the taxpayer to show that the statute clearly and beyond question is unconstitutional and invalid.⁴¹

Avoidance of double taxation as a ground of classification.

The answer to the first question above stated has been settled in numerous cases. Avoidance of the pyramiding of taxes or double taxation is a valid purpose; no unconstitutional discrimination results because one class, subject to double taxation, is allowed an exemption or

⁴¹*Madden v. Kentucky*, 309 U.S. 83, 88, 60 S.Ct. 406, 84 L.Ed. 590, 593; *Lindsley v. Natural Carbonic Gas Co.*, 220 U.S. 61, 78-79, 31 S.Ct. 337, 55 L.Ed. 369, 377-378; *Henderson Bridge Co. v. Henderson City*, 173 U.S. 592, 615, 19 S.Ct. 553, 43 L.Ed. 823; *City and County of San Francisco et al. v. Market St. Ry. Co.*, 98 F.2d 628, 633 (C.C.A. 9), cert. den. 305 U.S. 657, 59 S.Ct. 357, 83 L.Ed. 426, reh'g den. 306 U.S. 667, 59 S. Ct. 460, 83 L.Ed. 1062.

deduction to avoid it, while another class, not subject to double taxation, does not receive it.⁴² That the purpose of an exemption is to avoid double taxation may even be read into a statute though not clearly expressed.⁴³

The United States in relation to the composite tax structure.

The next question is whether sales to the United States must receive a reduced tax rate simply because there are sales which in consideration of other taxes do receive a reduced tax rate. To argue for this proposition is to set up an arbitrary privilege whereby the indirect interest of the United States in any taxable subject automatically confers upon it, at each stage of the taxing process separately considered, the most favorable tax treatment allowed to any, irrespective of the composite tax structure. Such is not the law. In *Tradesmen's National Bank v. Oklahoma Tax Commission*,⁴⁴

⁴²*Colgate v. Harvey*, 296 U.S. 404, 56 S.Ct. 252, 80 L.Ed. 299, and cases cited on first point, overruled on second point in *Madden v. Kentucky*, supra, 309 U.S. 83, 60 S.Ct. 406, 84 L.Ed. 590; *West Publishing Co. v. McColgan*, 27 Cal.2d 705, 166 P.2d 861, aff'd 328 U.S. 823, 66 S.Ct. 1378, 90 L.Ed. 1603, reh'g den. 329 U.S. 822, 67 S.Ct. 35, 91 L.Ed. 83; *Appeal on Fidelity-Philadelphia Trust Co.*, 354 Pa. 255, 47 A.2d 267 (1946); *Henneford v. Silas Mason Co.*, 300 U.S. 577, 586, 57 S.Ct. 524, 81 L.Ed. 814, 821; *Nesbitt v. Gill*, 227 N.C. 174, 41 S.E.2d 646, 653, aff'd per curiam Oct. 13, 1947, 332 U.S. _____, _____ S.Ct. _____, 92 L.Ed. Adv. Ops. 13.

⁴³*Carpenter v. Carman Distributing Co.*, 111 Colo. 566, 144 P.2d 770 (1943). An exemption of sales of substances becoming ingredients of services furnished by the purchaser was limited by statutory interpretation to cases where the purchaser would incur a tax upon his own use of the commodity. 51 *Am. Jur.* 340, sec. 286.

⁴⁴This case and *Pacific Co. v. Johnson*, 285 U.S. 480, 52 S.Ct. 424, 76 L.Ed. 893, discredit the earlier cases of *Miller v. Milwaukee*, 272 U.S. 713, 47 S.Ct. 280, 71 L.Ed. 487, and *Macallen Co. v. Massachusetts*, 279 U.S. 620, 49 S.Ct. 432, 73 L.Ed. 874, which appellant relied upon in the lower court, but apparently no longer relies upon.

309 U. S. 560, 567, 60 S.Ct. 688, 84 L.Ed. 947, there was involved a franchise tax on a national bank measured by net income. Such a tax was expressly restricted by Act of Congress to a rate not higher than "the highest of the rates * * * assessed upon mercantile, manufacturing, and business corporations" doing business within the state. National banks were required to *include* in the measure of the tax the interest from tax-immune federal securities, and so were State Banks and Morris Plan Companies. Other types of corporations were taxed upon their net income *excluding* interest from tax-immune federal securities. The court held this was not an invalid discrimination. The issue "turns upon an examination of the whole tax structure of the state", the court said.⁴⁵ The corporations free from net income tax on the revenue of tax-immune federal bonds were required to include those bonds in the value of their capital stock subject to a separate corporate license tax, and with few exceptions, the total taxes paid exceeded the total imposed on national banks. The court held that:

"* * * considering all the taxes imposed * * * the scheme of taxation adopted by Oklahoma does not discriminate against national banking associations."

p. 568.

The Supreme Court of Hawaii followed the same method. It balanced against the 1½% paid upon a sale to the United States, its post exchanges and ships' service stores, the ¼ of 1% paid upon a sale to a li-

⁴⁵p. 568.

censed merchant, plus the 1½% added before the goods reach the consumer through taxation of the sale by the merchant, and found that this totaled 1¾%, or more than the tax on the sale to the United States, its post exchanges and ships' service stores.

Appellant attacks the use of this method by the Hawaii court (Br. 58-59). Appellant seems to forget that it is the burden on the United States which he assails, and that to measure the economic burden by the same yardstick as if it were actually a tax is as favorable consideration of his contention as he can expect. The alternative would be to disregard the economic burden altogether.

Since the composite tax structure is the yardstick, it follows that the power to differentiate in rates upon consideration of other taxes is not one which can be exercised arbitrarily, and appellee's fear that this power will be used destructively (Br. 57) is an imaginary one.⁴⁶

⁴⁶The dissenting judge, instead of recognizing that the total of taxes charged to others is a ceiling on the amount of economic burden on the United States, thought that the United States must receive a *positive advantage* in the form of a 1½% differential between the combined economic and tax burden on retail merchants and the economic burden on the post exchanges of the United States. (R. 227.) Appellant too argues that post exchanges must have an advantage over retail merchants (Br. 60). No authority is cited for this theory, which would call for absurd results. For example, in the case of a tax imposed on the sale and the storage of gasoline, but not both (cf. *Gregg Dyeing Co. v. Query*, 286 U.S. 472, 52 S.Ct. 631, 76 L.Ed. 1232), no tax could be collected on the sale of gasoline to the United States because the United States could not have been taxed on the storage, and according to the theory advanced, it would be necessary to give the United States an advantage in the amount of this tax exemption.

Wilson v. Cook, supra,⁴⁷ affords a decisive answer to appellant's claim of discrimination. As previously noted there was before the court the contention that a tax on the privilege of purchasing timber from the United States and severing the timber from its lands laid an unconstitutional burden on the United States. This tax was required to be collected by the purchaser from the owner of the timber land, by withholding from the proceeds of the sale. The court held that whether or not this procedure could be followed where the company was purchasing from the United States, the tax assessed against the company did not impose an unconstitutional burden on the United States. It said:

“* * * We obviously do not by our judgment against the plaintiffs [Wilson Company] impose the tax on the Government. Their property alone is subject to the lien of the present judgment and to execution issued under it. They cannot recover the amount of the judgment from the Government unless the Constitution permits. And if it forbids they obviously will not collect the tax. *In neither case does our judgment impose any burden on the United States.* * * *” (Italics added).

pp. 484-485.

Hence, Wilson Company could not rely on the federal immunity even if it alone of all timber companies, solely because it was dealing with the United States, was prevented from passing on the tax by withholding it from the proceeds. As a result, it would be required to itself pay a tax because it was dealing with the

⁴⁷327 U.S. 474, 66 S.Ct. 663, 90 L.Ed. 793 (1946).

United States, which other timber companies did not pay because they passed it on. The possible discrimination against those dealing with the United States was not overlooked. Mr. Justice Rutledge, dissenting, urged it upon the court. The six member majority of the court (a seventh justice concurring in the result) found the discrimination point immaterial to the question before it, which was the contention that the tax on Wilson Company laid an unconstitutional burden on the United States. The majority of the court pointed out⁴⁸ that the argument against application of the tax to Wilson Company without recourse against the government, when other companies had recourse against their vendors, *would lie under the equal protection clause*,⁴⁹ not the federal immunity doctrine.

The action of the majority of the court in the *Wilson* case obviously was correct under the rule that the composite tax structure is the yardstick. The economic burden on the United States caused by the fact that one purchasing from it must pay a tax, would not exceed the tax withheld from other timber owners.

Kaiser Company v. Reid, supra,⁵⁰ is most informative. The United States appeared in the case as an

⁴⁸p. 485.

⁴⁹So far as the equal protection clause (properly speaking, since the case arises in a territory, the due process clause) may be involved here, the valid purpose to avoid the pyramiding of tax or double taxation (discussed supra under the caption "Avoidance of double taxation as a ground of classification", pp. 35 to 36), and the proper making of classifications to carry out this valid purpose (discussed infra under the caption "The alleged juridical discrimination", pp. 48 to 50), answer any such contention.

⁵⁰30 Cal. Adv. 614, 184 P.2d 879 (1947).

intervenor. Significantly, the case has not been taken to the Supreme Court of the United States.

Kaiser Company was the lessee of shipyards and facilities owned by the United States. The company operated this property under a cost-plus contract with the United States. Under California law a fee simple is subject to an *ad valorem* property tax. If the fee simple is taxed that assessment includes all of the separate interests in the property. However, if the fee simple is exempt, separate possessory interests are taxed to those holding them.⁵¹

There was internal evidence of the California practice in the *Kaiser* case. As to one shipyard, the land was privately owned and leased to the company for use under its contract with the United States. In this instance the private owner was assessed on the fee simple, and Kaiser Company was assessed only on its possessory interest in the government owned facilities. Where the United States owned both the land and the facilities Kaiser Company was assessed on its possessory interest in both.

The assessments were upheld, and the contention that they violated the federal government's immunity from taxation was denied, with citation of *United States v. Allegheny County*, supra,⁵² in which the Supreme Court had left open the right to tax the possessory interest.

⁵¹This practice was attacked as discriminatory in the earlier case of *Hammond Lumber Co. v. County of Los Angeles*, 104 Cal. App. 235, 285 Pac. 896; it was upheld as not discriminatory since the leasehold interest was assessed in all cases where the fee was exempt.

⁵²322 U.S. 174, 64 S.Ct. 908, 88 L.Ed. 1209.

To summarize the foregoing: Under the California system only those who lease from the United States and other exempt owners must pay a tax. Those who lease from taxable owners pay no tax. Obviously a less favorable rent can be obtained by the United States and other exempt owners than can be obtained by taxable owners. However, considering the composite tax structure, there is no discrimination. The loss in rent which the exempt owner may suffer is no greater than the tax which the private owner must pay.

The California court pointed out that the treatment of lessees of the federal government was no different from the treatment of lessees of the state and city governments. This is reminiscent of the argument made in and sustained by the lower court, and set forth *infra*⁵³ that Hawaii treats all sales to exempt purchasers the same.

S.R.A. Inc. v. Minnesota, *supra*,⁵⁴ is very similar to the *Kaiser Co.* case. The *S.R.A.* case involved an ad valorem property tax assessed against one holding an abandoned post office site under a contract of purchase from the United States. Minnesota pays heed to an uncompleted land purchase agreement only when the vendor is exempt, in which event the purchaser is taxed,⁵⁵ or when failure to consider the contract would deprive the property of a charitable or other exemp-

⁵³See discussion under the caption "The alleged juridical discrimination", pp. 48 to 50.

⁵⁴327 U.S. 558, 66 S.Ct. 749, 90 L.Ed. 851 (1946).

⁵⁵Minnesota Statutes 1941, secs. 273.19, 273.21, 92.51.

tion to which it is entitled.⁵⁶ There was internal evidence of this practice in the case,⁵⁷ though it was not commented upon.

It was argued that to sustain the tax on the purchaser would injuriously affect the United States. The court denied this contention saying:

“There is a suggestion that to hold United States property subject to state taxation pending the completion of payment will injuriously affect its salability and therefore interfere with the Government’s handling of its affairs. Our recent cases have disposed of this economic argument in a way which is contrary to petitioner’s contention. *Alabama v. King & Boozer*, 314 U.S. 1, and cases cited.”

p. 570.

The alleged inclusion of federal activities in the measure of the tax.

Appellant relies upon *Mayo v. United States*, supra,⁵⁸ *United States v. Allegheny County*, supra,⁵⁹ and *Missouri v. Gehner*.⁶⁰ In the *Mayo* case the tax was imposed directly on the United States for its activity of bringing commercial fertilizer into Florida. In the *Allegheny County (Mesta Machines Co.)* case, the tax was imposed on a lessee from the United States measured by more than his possessory interest in the prop-

⁵⁶*Village of Hibbing v. Commissioner of Taxation*, 217 Minn. 528, 14 N.W.2d 923.

⁵⁷The decision in *Village of Hibbing v. Commissioner of Taxation*, supra, preceding note, was cited and commented upon in the Minnesota decision under review in the *S.R.A.* case. 219 Minn. 493, 18 N.W.2d 442.

⁵⁸319 U.S. 441, 63 S.Ct. 432, 87 L.Ed. 1504 (1943) (Br. 35).

⁵⁹322 U.S. 174, 64 S.Ct. 908, 88 L.Ed. 1209 (1944) (Br. 36, 38).

⁶⁰281 U.S. 313, 50 S.Ct. 326, 74 L.Ed. 870 (1930) (Br. 59).

erty, and hence inclusive of the interest of the United States. In the *Gehner* case the vice of the tax was that the federal bonds were not disregarded.⁶¹ The tax was laid on net value, arrived at by the deduction of reserves. Since the deduction for reserves was reduced by part of the amount of federal bonds, obviously this amount of federal bonds was added to the net value and was taxed.

This leads to the question whether the sales made by the post exchange,⁶² a federal activity, were or were not disregarded. The dissenting judge thought they were not disregarded (R. 221), and appellant so argues (Br. 54). Such is not the case.

To illustrate: Suppose the Hawaii law imposed a tax of, first, $1\frac{3}{4}\%$ upon all sales to retail merchants for resale with no second tax levied, the second tax being included in the measure of the first tax;⁶³ secondly, $1\frac{1}{2}\%$ upon all sales to the territorial and federal governments and exempt institutions, irrespective of intended resale, and upon all sales to consumers, that is to say, wherever there was no second sale or it was not to be included in the measure of the tax. In such a case appellant would insist upon being classed with the second group.⁶⁴ He would rightly argue that it

⁶¹281 U.S. at p. 322.

⁶²This term is used here and below as inclusive of ships' service stores.

⁶³This is the effective rate under the actual law since $\frac{1}{4}$ of 1% on the first sale and $1\frac{1}{2}\%$ on the second sale total $1\frac{3}{4}\%$.

⁶⁴The dissenting judge thought that the tax exempt status was the thing to be disregarded, not the federal resale (R. 221). The illustration shows the error of this method. The tax exempt status must be kept in view, and the federal resale accordingly disregarded.

was no business of the Territory of Hawaii what the federal government did with the goods,⁶⁵ that if sales to post exchanges were included in the first group the Territory would be wrongfully considering and taking into account a federal activity, namely the intended resale at the post exchange.

We fail to see why the situation is any different because under the actual Hawaii law, the tax is, first $\frac{1}{4}$ of 1% upon the first sale to, and $1\frac{1}{2}\%$ upon the second sale by, a retail merchant; secondly, $1\frac{1}{2}\%$ upon all sales to the territorial and federal governments and exempt institutions, irrespective of intended resale, and upon all sales to consumers, that is to say, wherever the first sale is the last taxable sale.

Hence, in answer to the second question put at the beginning of this point: In a tax system devised to avoid undue pyramiding of the tax or double taxation, must the Territory segregate, and give consideration to an activity of the United States, which for taxation purposes it is required to disregard, we say emphatically, "No."

Only if the Territory charged $1\frac{3}{4}\%$ upon sales to non-taxable vendees for resale, would the exempt federal activity be included in the measure of the tax in violation of the *Mayo*, *Mesta Machine Co.* and *Gehner* cases. Such tax would be $\frac{1}{4}$ of 1% more than on a

⁶⁵*Jefferson County v. United States*, *supra*, 164 F.2d 184 (C.C.A. 5th 1947), holding that the use made of property by the federal government cannot be considered by a local taxing authority; Powell, "*The Waning of Intergovernmental Tax Immunities*", *supra*, 58 Harv.L.R. 633, 646, 656.

sale to one making no resale, and hence would wrongfully take into account the resale activities of the federal government, with which the Territory has no concern. *The touchstone is that rate of tax upon sales to consumers.* Since the rate upon sales to post exchanges is the same as upon sales to consumers, the federal activity in reselling the goods truly is disregarded.

The alleged factual discrimination.

Appellant claims that the post exchanges are in competition with others for goods at the wholesale level (Br. 54-56, 60-61). The same argument could be made as to any department of the United States government. These government departments, like the post exchanges, buy in wholesale lots and at wholesale prices. Therefore they too are buying in the wholesale market in the trade sense of that term. Yet appellee does not claim that other sales to the United States should be rated at $\frac{1}{4}$ of 1%. He recognizes that when the government department is a consumer the rate of $1\frac{1}{2}\%$ applicable to sales to other consumers is proper. Hence, he does not insist, and indeed he could not, that differentiations in rate amongst sales which the trade considers "wholesale," are forbidden. What he does insist is that no differentiation in rate can be made amongst sales for resale.

What is there in the intended resale that marks sales to post exchanges for more favorable treatment than sales to the War Department itself? The conten-

tion is that the post exchanges *are in competition with retail merchants* for business (Br. 56).

In the first place the claim is false. Post exchanges are not in competition with retail merchants for business. As characterized by the Supreme Court of the United States:⁶⁶

“* * * The object of the exchanges is to provide convenient and reliable sources where soldiers can obtain their ordinary needs at the lowest possible prices.”

The United States is a government of delegated powers. All of its functions necessarily are governmental.⁶⁷ In this it differs from a state, whose functions are not necessarily governmental.⁶⁸

In the Supreme Court case⁶⁹ the profits of a post exchange, if any, were treated as incidental. If supplies are retailed by business houses in a convenient and satisfactory manner as cheaply as the government could do it, it is not the function of the post exchanges to go out and take the business away from them. Nowhere in the Supreme Court case or the Army Regulations (Ex. D, R. 41-97) is such a competitive purpose contemplated or sanctioned.

⁶⁶*Standard Oil Co. v. Johnson*, *supra*, 316 U.S. 481, at pp. 484-5.

⁶⁷*Federal Land Bank v. Bismarck Co.*, *supra*, 314 U.S. 95, 102, 62 S.Ct. 1, 86 L.Ed. 65; Powell, “*The Waning of Intergovernmental Tax Immunities*”, *supra*, 58 Harv.L.R. 633, 646, 656.

⁶⁸Whether or not the word “proprietary” is still in good repute as descriptive of certain non-governmental functions of the states is not material (cf. Br. 49, citing *New York v. United States*, 326 U.S. 572, 66 S.Ct. 310, 90 L.Ed. 326).

⁶⁹*Supra*, note 66.

Secondly, the complaint is one which should come from the post exchanges to merit serious consideration. They do not make it. Obviously, if not satisfied with the prices of goods in the Territory of Hawaii they will purchase elsewhere.⁷⁰ This is appellant's real complaint; it lies to the burden put on local business in competition with mainland suppliers. Such a complaint must be addressed to the legislature, not the courts.

In the third place, if competition did exist between post exchanges and retail merchants, the argument based thereon already has been answered, upon consideration of the composite tax structure.⁷¹

In the fourth place, in so far as the tax may be reflected in the price paid by the post exchange, and may cause the service afforded by the post exchanges not to be as cheap as it otherwise would be, that is an economic burden which the Supreme Court has held the United States must assume.

The alleged juridical discrimination.

Appellee-tax commissioner agrees that a classification must have a valid purpose and be properly made to carry out that purpose.⁷² Appellee has shown that the purpose of the classification made by the leg-

⁷⁰39 Ops. Atty. Gen. 316, 322, *supra*.

⁷¹Discussed *supra* under the caption "The United States in relation to the composite tax structure", pp. 36 to 43.

⁷²The cases cited in Appellant's Br. 53 are cases in support of this general principle.

islature is to avoid undue pyramiding of the tax or double taxation, and that this is a valid purpose.⁷³ Appellee further has shown that the classification has been properly made to carry out that purpose.⁷⁴ To summarize: Sales to the post exchanges are classed by the statute with other sales to the federal government, and with sales to the territorial government and agencies thereof, charitable institutions, hospitals, fraternal benefit societies, public utilities, users and consumers, and others not themselves subject to the tax. This class includes the instances in which no second taxable sale will occur, either because there will be no second sale (e.g., sales to the federal and territorial government for their use, and to other users and consumers), or because though a second sale will occur it will not be taxable and hence is disregarded (e.g., sales of food to school cafeterias, sales of stoves and refrigerators to public utilities for resale, sales of medicines to hospitals for resale, and sales to the post exchanges). These are all instances in which there is no occasion to allow a reduced rate, since there is no double taxation to be avoided.

This court already has held that a classification having a valid purpose may be applied to those dealing with the federal government the same as to others. In *Yerian v. Territory*,⁷⁵ supra, this court summarily dis-

⁷³Supra, point 1 of this part B, pp. 28 to 34, and discussion under the caption "Avoidance of double taxation as a ground of classification", p. 35.

⁷⁴Supra, note 73.

⁷⁵130 F.2d 786, 790.

posed of the contention that to require federal employees to file tax returns discriminated against the federal government, pointing out that the same requirement applied to all employees of non-resident employers. This was in accordance with the general rule that if those who deal with the federal government are treated *as fairly as others similarly situated*, there is no ground for complaint.⁷⁶

CONCLUSION.

Appellee-tax commissioner respectfully submits that the Territory of Hawaii lawfully can include in the measure of a privilege tax upon the business of selling tangible personal property in the Territory, the gross proceeds of sales made to the United States, and the post exchanges and ships' service stores which are integral parts thereof. The Territory was created by

⁷⁶Thus in *Wood v. Tawes*, 181 Md. 155, 28 Atl. 2d 850, 854 (1942), cert. den. 318 U.S. 788, 63 S.Ct. 982, 87 L.Ed. 1154, the claim of certain federal officers, taxed on their compensation, that there was discrimination against them, was denied because they failed to show that state officers in comparable positions were treated more favorably.

In *Wood Bros. v. Bagley*, 232 Iowa 902, 6 N.W.2d 397 (1942), the law provided that there should be refunded to the consumer the fuel tax, in the amount of three cents per gallon, paid on fuel which ultimately was not used for motor vehicle transportation. As an exception to this refund provision the law provided that if the fuel had been used for construction work paid for from public funds there would be no refund. As a result, a contractor dealing with the government was required to pay three cents more per gallon on fuel used in construction work for the government than on fuel used in other construction work. It was held that the exception applied where the construction work was paid for from federal funds the same as where paid for from state or county funds.

Congress as a sovereign government with full power to impose taxes, and its power to tax the United States and its instrumentalities is as great as, though no greater than, the powers of the states with respect to such taxation. The inclusion of gross proceeds of sales to the United States, its post exchanges and ships' service stores, in the measure of a privilege tax upon the business of selling tangible personal property in the Territory, has only an economic effect upon the federal government, and does not constitute the tax an invalid burden upon or interference with federal activities. The *Panhandle* line of cases has been overruled.

Appellee-tax commissioner further submits that the Territory of Hawaii, in a privilege tax act which taxes every sale, service or other activity, can avoid the undue pyramiding of the tax by prescribing a lower rate where a second taxable activity is to follow. In such a tax system, the Territory need not segregate and give consideration to an activity of the United States which for taxation purposes it is required to disregard; such federal activity may and should be disregarded for all purposes. The Supreme Court of Hawaii correctly interpreted the tax statute as classifying sales to post exchanges and ships' service stores with sales to the federal and territorial governments, charitable institutions, hospitals, fraternal benefit societies, public utilities, users and consumers, and others where no second taxable activity occurs. This classification properly carries a tax rate of $1\frac{1}{2}\%$ in common with other business activities, in

contradistinction to sales to licensed retail merchants, where to avoid undue pyramiding of the tax a tax rate of $\frac{1}{4}$ of 1% is allowed.

Dated, Honolulu, Territory of Hawaii, March 30, 1948.

Respectfully submitted,

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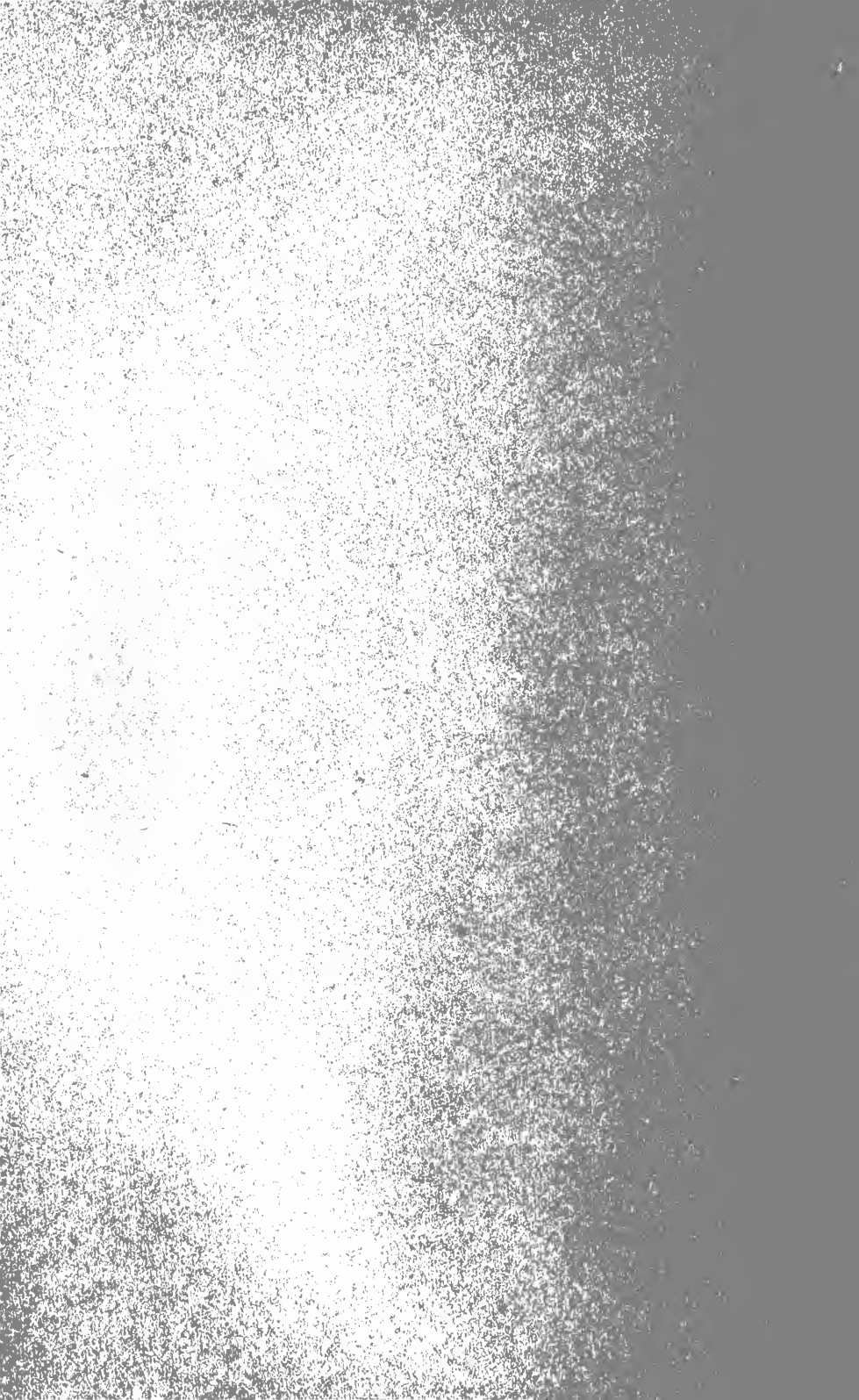
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(Appendix Follows.)

Appendix.



Appendix

ACT 141 (SERIES A-44) SESSION LAWS OF HAWAII 1935,
AS AMENDED TO AND INCLUDING THE SESSION LAWS OF
HAWAII, 1943.

Italics indicate provisions added by Act 81 (Series A-54) Session Laws of Hawaii, 1943.

Section 1. *Definitions.* When used in this Act, unless otherwise required by the context:

(1) "Commissioner" or "tax commissioner" shall mean the tax commissioner of the Territory of Hawaii.

(2) "Person" or "company" shall include every individual, partnership, society, unincorporated association, joint adventure, group, hui, joint stock company, corporation, trustee, executor, administrator, trust estate, decedent's estate, trust or other entity, whether said persons are doing business for themselves or in a fiduciary capacity, and whether the individuals are residents or non-residents of the Territory, and whether the corporation or other association is created or organized under the laws of the Territory or of another jurisdiction.

(3) "Tax year" or "taxable year" means either the calendar year, or the taxpayer's fiscal year when permission is obtained from the tax commissioner to use same as the tax period in lieu of the calendar year.

(4) "Sale" or "sales" includes the exchange of properties as well as the sale thereof for money.

(5) "Taxpayer" means any person liable for any tax hereunder.

(6) "Gross income" means the gross receipts, cash or accrued, of the taxpayer received as compensation for personal services and the gross receipts of the taxpayer derived from trade, business, commerce or sales and the value proceeding or accruing from the sale of tangible personal property, or service, or both, and all receipts, actual or accrued as hereinafter provided, by reason of the investment of the capital of the business engaged in, including interest, discount, rentals, royalties, fees, or other emoluments however designated and without any deductions on account of the cost of property sold, the cost of materials used, labor cost, taxes, royalties, interest or discount paid or any other expenses whatsoever. Provided, that every taxpayer shall be presumed to be dealing on a cash basis unless he proves to the satisfaction of the commissioner that he is dealing on an accrual basis and his books are so kept, or unless he employs or is required to employ the accrual basis for the purposes of the tax imposed by chapter 65 of the Revised Laws of Hawaii 1935 for any taxable year in which event he shall report his gross income for the purposes of this Act on the accrual basis for the same period.

(7) "Business" as used in this Act, shall include all activities, (personal, professional or corporate) engaged in or caused to be engaged in with the object of gain or economic benefit either direct or indirect, but shall not include casual sales.

(8) "Gross proceeds of sale" means the value actually proceeding from the sale of tangible personal property without any deduction on account of the

cost of property sold or expenses of any kind. The words "gross income" and "gross proceeds of sales" shall not be construed to include the gross receipts from the sale of bonds or other evidence of indebtedness or stocks or from the sale of real property; cash discounts allowed and taken on sales; the proceeds of sale of goods, wares or merchandise returned by customers when the sale price is refunded either in cash or by credit; or the sale price of any article accepted as part payment on any new article sold if the full sale price of the new article is included in the "gross income" or "gross proceeds of sales." And accounts found to be worthless and actually charged off for income tax purposes may, at corresponding periods, be deducted from gross proceeds of sale, or gross income, within this Act, so far as they reflect taxable sales made, or gross income earned after July 1, 1935, but shall be added to gross proceeds of sale or gross income when and if afterwards collected.

(9) "Service business or calling" shall include all non-professional activities engaged in for other persons for a consideration, which involve the rendering of a service as distinguished from the production or sale of tangible property, but shall not include the services rendered by an employee to his employer.

(10) "Wholesaler" or "jobber" shall apply only to a person doing a regularly organized wholesale or jobbing business, known to the trade as such, and only with respect to the following sales: (a) sales, to a licensed retail merchant or jobber, for purposes of resale; (b) sales, to a licensed manufacturer, of mate-

rial or commodities which are to be incorporated by such manufacturer into a finished or saleable product (including the container or package in which the product is contained) during the course of its preservation, manufacture or processing, including preparation for market, and which will remain in such finished or saleable product in such form as to be perceptible to the senses, which finished or saleable product is to be sold and not otherwise used by such manufacturer; or (c) sales, to a licensed contractor, of material or commodities which are to be incorporated by such contractor into the finished work or project required by the contract and which will remain in such finished work or project in such form as to be perceptible to the senses.

Provided, that in the event the consumption tax law shall be finally held by a court of competent jurisdiction to be unconstitutional or invalid in so far as it purports to tax the use or consumption of tangible personal property imported into the Territory in interstate or foreign commerce or both, then and in such event wholesalers and jobbers shall be taxed thereafter under this Act in accordance with the following definition (which shall supersede the preceding paragraph otherwise defining "wholesaler" or "jobber"), to-wit:

"Wholesaler" or "jobber" shall mean a person, or a definitely organized division thereof, definitely organized to render and rendering a general distribution service which buys and maintains at his or its place of business a stock or lines of merchandise

which he or it distributes; and which, through salesmen, advertising or sales promotion devices, sells to licensed retailers, or to institutional, or licensed commercial or industrial users, in wholesale quantities and at wholesale rates.

(11) The term “producer” shall mean and include any person engaged in the business of raising and producing agricultural, animal or poultry products in their natural state, or in producing natural resource products, or engaged in the business of fishing, who sells agricultural, animal or poultry products in their natural state, or butchered and dressed, or the natural resource products, or the fish, for resale or to be incorporated and remain in finished manufactured products, or in the finished work required under a construction contract.

(12) “Retail” means the sale of tangible personal property, other than by a wholesaler as such within the definition of this Act, for consumption or use by the purchaser and not for resale.

(13) “Retailer” shall mean any person who sells, other than as a wholesaler within the definition of this Act, tangible personal property for consumption or use by the purchaser and not for resale.

(14) “Contractor” shall include, for purposes of this Act, every person engaging in the business of contracting to erect, construct, repair or improve buildings or structures, of any kind or description, including any portion thereof, or to make any installation therein, or to make, construct, repair or improve any

highway, road, street, sidewalk, ditch, excavation, fill, bridge, shaft, well, culvert, sewer, or water system, drainage system, dredging or harbor improvement project, electric or steam rail, lighting or power system, transmission line, tower, dock, wharf, or other improvements. *“Federal cost-plus contractor” means a contractor having a contract with the United States or an instrumentality thereof, where, by the terms of the contract, the United States or such instrumentality agrees to reimburse the contractor for the cost of material, plant or equipment used in the performance of the contract and for taxes which the contractor may be required to pay with respect to such material, plant or equipment, whether the contractor’s profit is computed in the form of a fixed fee or on a percentage basis; and also means a sub-contractor under such a contract, who also operates on a cost-plus basis.*

(15) *“Auditor” means the auditor of the Territory of Hawaii.*

(16) The term *“engaging”* as used in this Act with reference to engaging or continuing in business shall also include the exercise of corporate or franchise powers.

(17) The word *“penalty”* or *“penalties”*, when used in connection with the additions to the tax imposed for delinquency in payment, shall include interest as well. (L. 1935, c. 141, s. 1; am. L. 1941, c. 265, s. 1; am. L. 1943, c. 81, s. 1.)

Section 2. *Imposition of tax; rates.** I. There is hereby levied and shall be assessed and collected annually privilege taxes against the persons on account of their business and other activities in this Territory measured by the application of rates against values, gross proceeds of sales or gross income, as the case may be, as follows:

A. *Tax on manufacturers.* (1) Upon every person engaging or continuing within this Territory in the business of manufacturing, compounding, canning, preserving, packing, milling, processing, refining or preparing for sale, profit or commercial use, either directly or through the activity of others, in whole or in part, any article or articles, substance or substances, commodity or commodities, the amount of such tax to be equal to the value of the articles, substances or commodities, manufactured, compounded, canned, preserved, packed, milled, processed, refined or prepared, for sale, as shown by the gross proceeds derived from the sale thereof by the manufacturer or person compounding or preparing the same (except as hereinafter provided), multiplied by the respective rates as follows:

Millers or processors of sugar, raw or refined, or sugar by-products, one and one-quarter ($1\frac{1}{4}$) per cent; canneries, one and one-quarter ($1\frac{1}{4}$) per cent; all other manufacturers on whose gross income a tax

*Commencing July 1, 1939 all $1\frac{1}{4}\%$ rates were raised to $1\frac{1}{2}\%$ by order of the Governor. (See subsection III relating to increase or decrease of rates.)

is not otherwise levied in this Act, one-quarter ($\frac{1}{4}$) of one per cent.

(2) The measure of the tax on manufacturers is the value of the entire product manufactured, compounded, canned, preserved, packed, milled, processed, refined or prepared, in this Territory, for sale, profit or commercial use, regardless of the place of sale or the fact that deliveries may be made to points outside the Territory.

(3) If any person liable for the tax on manufacturers shall ship or transport his products, or any part thereof, out of this Territory without making sale of such products, the value of the products in the condition or form in which they existed immediately before entering interstate or foreign commerce shall be the basis for the assessment of the tax imposed in this section. The commissioner shall prescribe equitable and uniform rules for ascertaining such value; and the tax imposed on manufacturers shall be due and payable as of the date of such entry into interstate or foreign commerce, whether said products have been sold or not. If any person liable for the tax on manufacturers shall ship or transport his products, or any part thereof, outside of the Territory in an unfinished condition, the value of the products or articles in the condition or form in which they existed when shipped or transported out of the Territory and before they entered interstate or foreign commerce shall be the basis of assessment of the tax imposed on manufacturers and the commissioner shall prescribe equitable and uniform rules for ascertaining such value.

(4) In computing the tax levied on manufacturers where the gross proceeds of sales of such manufactured products are taken as the measure of the value of such products for the purpose of computing the tax, if such products shall have been sold on a delivered price, the actual transportation charges prepaid by the taxpayer or included in the invoice price on such manufactured products, to the place of delivery shall be deducted from the gross proceeds of sales used in determining the amount of the tax.

(5) Provided, however, that any person engaging or continuing in the business of refining sugar in the Territory, who purchases raw sugar for such refining, the seller of which raw sugar is taxable in respect to such sale under section 2, I-A, will be entitled to deduct from the amount of the value used for computing the tax, the amount paid by him for such raw sugar. The refiner shall show in his return the amounts of his purchase of such raw sugar and from whom purchased.

(6) In computing the tax levied under section 2, I-A, any person who by reason of the Agricultural Adjustment Act, or other Acts of Congress of the United States, includes as a part of his gross income a processing tax, or other similar tax, paid either to the federal or territorial governments, shall be entitled to deduct from the amount of the value used for computing the tax payable under section 2, I-A, hereof, the amount of the processing tax, or other similar tax, paid by him to the federal government; provided,

however, that this paragraph shall not be construed to entitle the taxpayer to deduct any sums that may be returned and retained as a benefit payment so-called or a like payment by virtue of the Agricultural Adjustment Act or other Acts passed by the Congress of the United States relating thereto.

B. Tax on retailers, wholesalers and producers. (1) Upon every person engaging or continuing within this Territory in the business of selling any tangible personal property whatsoever (not including, however, bonds or other evidence of indebtedness or stocks) there is likewise hereby levied, and shall be assessed and collected, a tax equivalent to one and one-quarter ($1\frac{1}{4}$) per cent of the gross proceeds of sales of the business; provided, however, that in the case of a wholesaler or producer, the tax shall be equal to one-quarter ($\frac{1}{4}$) of one per cent of the gross proceeds of sales of the business.

(2) Provided, that gross proceeds of sales of tangible property in interstate and foreign commerce shall constitute a part of the measure of the tax imposed on retailers and wholesalers, to the extent, under the conditions and in accordance with the provisions of the Constitution of the United States and the Acts of the Congress of the United States which may be now in force or may be hereafter adopted.

(3) Provided, however, that any person engaging or continuing in business as a retailer and a wholesaler or as a retailer and a producer shall pay the tax required on the gross proceeds of sales of each

such business at the rates specified, when his books are kept so as to show separately the gross proceeds of sales of each business; and when his books are not so kept he shall pay the tax as a retailer.

(4) A manufacturer or producer engaging in the business of selling his manufactured products at retail in this Territory shall be required to make returns of the gross proceeds of such retail sales and pay the tax imposed in this Act, for the privilege of engaging in the business of selling such products at retail in this Territory; and the value, or gross proceeds of sales, of such products, thus sold by the manufacturer or producer at retail and included in the measure of the tax imposed in this Act, shall be deducted from the gross income, or gross proceeds of sales, used in determining the measure of the tax imposed upon such manufacturer or producer as such.

(5) But a manufacturer or producer engaging in the business of selling his products to manufacturers, wholesalers, or licensed retailers, shall not be required to pay the tax imposed in this Act for the privilege of selling such products at wholesale. Nor shall any such manufacturer or producer be required to pay the tax imposed in this Act for the privilege of selling products for delivery outside of this Territory. But the gross income derived from the sale of such products to manufacturers, wholesalers, or licensed retailers, and the gross income derived from all sales of such products, for delivery outside of this Territory, shall be included in determining the measure of

the tax imposed upon such manufacturer or producer as such.

(6) Provided, further, that a taxpayer selling to a federal cost-plus contractor may make the election provided for by paragraph (3) of subsection C, and in any such case the tax shall be computed pursuant to the election, notwithstanding any provision of this subsection or subsection A to the contrary.

C. *Tax upon contractors.* (1) Upon every person engaging or continuing within this Territory in the business of contracting, the tax shall be equal to one and one-quarter ($1\frac{1}{4}$) per cent of the gross income of the business. Provided, however, that the rate of tax levied upon any such person measured by gross income received on account of uncompleted contracts, entered into prior to the effective date of this Act shall be eight-tenths of one per cent. All contracts shall be prima facie presumed to have been entered into subsequent to the effective date of this Act.

(2) Provided, however, that in computing the tax levied under this subsection C, there shall be deducted from the gross income of the taxpayer, so much thereof as has been included in the measure of the tax levied under subsection C (1) on other taxpayers; but any person claiming such deduction shall be required to show in his return the names of the persons paying the amount deducted hereunder.

(3) Provided, further, that in computing the tax levied under this subsection C against any federal

cost-plus contractor, there shall be excluded from the gross income of the contractor so much thereof as fulfills the following requirements:

(a) The gross income exempted shall constitute reimbursement of costs incurred for materials, plant or equipment purchased from a taxpayer licensed under this Act, not exceeding the gross proceeds of sale of such taxpayer on account of the transaction.

(b) The taxpayer making the sale shall have certified to the commissioner that he is taxable with respect to the gross proceeds of the sale, and that he elects to have the tax on such gross income computed as if the sale were made to the federal government direct.

D. Tax upon theaters, amusements, radio broadcasting stations, etc. (1) Upon every person engaging or continuing within this Territory in the business of operating a theater, opera house, moving picture show, vaudeville, amusement park, dance hall, skating rink, radio broadcasting station or any other place at which amusements are offered to the public, the tax shall be equal to one and one-quarter ($1\frac{1}{4}$) per cent of the gross income of the business.

(2) Provided, however, that where the rental paid for the use of films in any theater or moving picture house is included in the gross income by which the tax against the lessor of the films is measured under this Act, the amount of rental paid by the lessee operator to such lessor shall be deducted from the lessee

operator's gross income used in determining the measure of the tax imposed upon such operator under subsection D (1).

F. *Tax on service business.* Upon every person engaging or continuing within this Territory in any service business or calling not otherwise specifically taxed under this Act, there is likewise hereby levied and shall be assessed and collected a tax equal to one and one-quarter ($1\frac{1}{4}$) per cent of the gross income of any such business.

G. *Professions.* Upon every person engaging or continuing within this Territory in the practice of a profession, including those expounding the religious doctrines of any church, there is likewise hereby levied and shall be assessed and collected a tax equal to one and one-quarter ($1\frac{1}{4}$) per cent of the gross income of such practice or exposition.

H. *Tax on other business.* Upon every person engaging or continuing within this Territory in any business, trade, activity, occupation, or calling not included in the preceding subsections or any other provisions of this Act, there is likewise hereby levied and shall be assessed and collected, a tax equal to one and one-quarter ($1\frac{1}{4}$) per cent of the gross income thereof. This subsection shall apply to the gross income of persons taxable under other subsections hereof not derived from the exercise of privileges taxable thereunder.

II. Where delivery of any products is made by a taxpayer, taxable under this Act, to other affiliated companies or persons, or under other circumstances where the relation between the manufacturer or producer and the receiver of such products is such that the consideration paid, if any, is not indicative of the true value of the products delivered, the taxpayer shall pay the tax imposed by this Act for the privilege of engaging in the business of producing or manufacturing the products so delivered, measured by the value, corresponding as nearly as possible to the gross proceeds of sale of similar products, of like quality and character, by other persons, where no common interest exists between the buyer and seller but the circumstances and conditions are otherwise similar. If no such comparable sales exist between non-affiliated buyers and sellers, the commissioner shall prescribe equitable and uniform rules for ascertaining such value.

III. Before the 15th day of June of each year the director of the bureau of the budget shall prepare and submit to the treasurer an estimate of the amount of moneys required for the purpose of meeting the estimated probable expenditures during the next fiscal year, and if the amount of money required is less than the amount of money estimated to be available, the treasurer may, with the written approval of the governor, decrease the rate of one and one-quarter per cent ($1\frac{1}{4}\%$) fixed by section 2-I to such extent that the estimated amount to be raised hereunder will only be sufficient to meet the required expenditures.

But if the estimate of the moneys required, in addition to all other moneys estimated to be available for the purpose of meeting the estimated probable expenditure during the next fiscal year, shall be greater than the amount of money available by virtue of the taxes imposed by this Act at the rates fixed by section 2-I thereof, then the treasurer may, with the written approval of the governor increase the rate of one and one-quarter per cent ($1\frac{1}{4}\%$) fixed by said section 2-I to such extent, not exceeding an additional one-quarter of one per cent ($\frac{1}{4}\%$), that the estimated amount to be raised hereunder will be sufficient (within the limit of such increase) to meet the required expenditures.

Such increase or decrease in rate shall apply to taxes accruing during the said fiscal year.

IV. If any person, other than persons liable to the tax on manufacturers as provided by part A of subsection 1 of this section, is engaged in business both within and without the Territory, and if, under the Constitution or laws of the United States the entire gross income of such person cannot be included in the measure of this tax, there shall be apportioned to the Territory and included in the measure of the tax that portion of the gross income which is derived from activities within the Territory, to the extent that such apportionment is required by the Constitution or laws of the United States. In the case of a tax upon the production of property in the Territory such apportionment shall be determined as in the case of the tax on manufacturers. In other cases, if and to the extent

that such apportionment cannot be accurately made by separate accounting methods, there shall be apportioned to the Territory and included in the measure of this tax that proportion of the total gross income, so requiring apportionment, which the cost of doing business within the Territory, applicable to such gross income, bears to the cost of doing business both within and without the Territory, applicable to such gross income. (L. 1935, c. 141, s. 2; am. L. 1937, c. 128, s. 1; am. L. 1939, c. 252, s. 1; am. L. 1941, c. 115, s. 1; am. L. 1943, c. 81, s. 1.)

Section 3. *Interstate and foreign commerce. Federal agencies.* In computing the amounts of any tax imposed under this Act, there shall be excepted from the gross proceeds of sales or gross income, so much thereof as is derived from sales of tangible property in interstate and foreign commerce, which under the Constitution of the United States, the Territory of Hawaii, is, or may hereafter be, prohibited from taxing, or is derived from any sales made to the United States government, its departments or agencies, which is, or may hereafter be, exempted from taxation under the Constitution of the United States or the Organic Act of the Territory; provided, however, that if and when the Congress of the United States shall permit the Territory of Hawaii to impose a privilege tax upon gross proceeds of sales or gross income derived from sales of tangible personal property in interstate and foreign commerce, or from sales made to the United States government, its departments or agencies, in either such event the exceptions and exemptions by this section provided, shall not apply.

Section 4. *Exemptions.* The provisions of this Act shall not apply to:

(1) The following persons:

(a) National banks; (b) Banks on whose shares of stock or net worth a tax is levied under the provisions of an Act of the legislature of the Territory of Hawaii at its 1935 session, entitled: "An Act to provide for the taxation of the shares of the capital stock of banks; and for the taxation of foreign banks; to provide for the ascertainment, assessment, collection and disposition of such tax; to provide penalties for violations of the terms thereof and to repeal chapter 62, Revised Laws of Hawaii 1935, and all other laws or parts of laws inconsistent herewith;" (c) Public utilities (as that term is defined in the Revised Laws of Hawaii 1935, section 7940), with respect to their public utilities business, upon the gross income from which they pay an annual tax under the provisions of the Revised Laws of Hawaii 1935, chapter 69; (d) Public utilities owned and operated by the Territory or any county or city and county or other political subdivisions thereof; (e) Insurance companies which pay the Territory of Hawaii a tax upon their gross premiums under the provisions of the Revised Laws of Hawaii 1935, chapter 224; (f) Fraternal benefit societies, orders or associations, operating under the lodge system, or for the exclusive benefit of the members of the fraternity itself, operating under the lodge system, and providing for the payment of death, sick, accident or other benefits to the members of such societies, orders or associations, and to their dependents;

(g) Corporations, associations or societies organized and operated exclusively for religious, charitable, scientific or educational purposes; (h) Business leagues, chambers of commerce, boards of trade, civic leagues and organizations operated exclusively for the benefit of the community and for the promotion of social welfare, and from which no profit inures to the benefit of any private stockholder or individual; (i) Hospitals, infirmaries and sanatoria; (j) Cooperative associations now or hereafter incorporated under and pursuant to the provisions of the Revised Laws of Hawaii 1935, chapter 220; provided, however, that the exemption herein provided shall apply only to the gross income derived from its non-profit activities; (k) Building and loan associations, with respect only to interest received by them on loans to members; (l) Lepers and kokuas, with respect to business within the county of Kalawao;

Provided, however, that the exemptions of this section 4 (1) shall apply only to the gross income of those persons enumerated in section 4 (1) (f) to section 4 (1) (i), both inclusive, from non-profit activities.

Provided, further, that the exemptions enumerated in this section 4 (1) from (f) to (k), both inclusive, shall apply only to those persons who (1) shall have registered with the tax commissioner on or before January 31 of each calendar year, or within one month after the commencement of business, by filing a written application for registration in such form as the commissioner shall prescribe, and (2) shall have paid for such registration an annual fee of one dollar

(\$1.00), and (3) shall have had the exemption allowed by the commissioner or by a court or tribunal of competent jurisdiction upon appeal from any assessment resulting from disallowance of the exemption by the commissioner, and (4) shall make returns of gross income and gross proceeds of sales as required by this Act.

In order to obtain allowance of an exemption an application for exemption shall be filed in the form of an affidavit or affidavits setting forth in general all facts affecting the right to the exemption and such particular facts as the commissioner may require, to which shall be attached such records, papers and other information as the commissioner may prescribe. Such application for exemption shall be filed on or before March 31 of the first year of registration or within three months after the commencement of business. In the event of allowance of the exemption no further application therefor need be filed unless there be a material change in the facts, but such person nevertheless shall register annually. In the event of disallowance of the exemption a license may be obtained without payment of a further fee, and in the event the registrant has a license under this Act no further fee shall be required for registration under this section.

The commissioner for good cause may extend the time for registration or the time for filing an application for exemption, but such extension or extensions shall not aggregate more than a total of two months.

(2) The following gross income or gross proceeds of sales:

(l) Amounts received under life insurance policies and contracts paid by reason of the death of the insured; (m) Amounts received (other than amounts paid by reason of the death of the insured) under life insurance, endowment or annuity contracts, either during the term or at maturity, or upon surrender of the contract; (n) Amounts received by any person under any accident insurance or health insurance policy or contract or under workmen's compensation Acts or employers' liability Acts, as compensation for personal injuries, death or sickness, including also the amount of any damages or other compensation received, whether as a result of action or by private agreement between the parties on account of such personal injuries, death or sickness; (o) The value of all property of every kind and sort acquired by any person by gift, bequest or devise, and the value of all property acquired by any person by descent or inheritance; (p) Amounts received by any person as compensatory damages for any tort injury to him, or to his character or reputation, or received by any person as compensatory damages for any tort injury to or destruction of property, whether as the result of action or by private agreement between the parties; provided, however, that amounts received by any person as punitive damages for tort injury or breach of contract injury shall be included in gross income; (q) The amounts collected by distributors as a fuel tax on "liquid fuel" imposed by the provisions of the Revised Laws of Hawaii 1935, chapter 64 and the amounts collected by such distributors as a fuel

tax imposed by any Act of the Congress of the United States; (r) The amount received by any person as a benefit payment so-called or like payments by virtue of the Agricultural Adjustment Act or other acts passed by the Congress of the United States relating thereto and disbursed to others as such benefit payment; provided that the commissioner may by rule require any deductions to be set forth specifically by the taxpayer in his return; (s) Amounts received as salaries or wages for services rendered by an employee to an employer; (t) Amounts received as alimony and other similar payments and settlements; (u) The amounts collected by retailers and wholesalers as a tax on liquor imposed by the provisions of Act 222, Session Laws of Hawaii 1939. (L. 1935, c. 141, s. 4; am. L. 1939, c. 47, s. 1; am. L. 1941, c. 265, s. 2; am. L. 1943, c. 81, s. 1.)

Section 5. *Computation of tax, payment.* (1) The taxes levied hereunder shall be payable in monthly installments on or before the expiration of twenty days from the end of the month in which they accrue. The taxpayer shall, within twenty days from the expiration of each month, make out and sign an estimate of the tax for which he is liable for such month and transmit the same, together with a remittance, in the form required by section 12 of this Act, for the amount of the tax, to the office of the appropriate territorial divisional tax assessor hereinafter designated. Any person registered or required to be registered under section 4 of this Act, shall file monthly returns of gross income and gross proceeds of sales, but while

his application for exemption is pending before the tax commissioner or if it be allowed no payment of tax need accompany the return.

(2) The commissioner for good cause may extend the time for making any return required under this section, and may grant such reasonable additional time within which to make such return as he may deem proper, but the time for filing such return shall not be extended beyond the twentieth day of the second month next succeeding the regular due date of such return. (L. 1935, c. 141, s. 5; am. L. 1941, c. 265, s. 3.)

Section 6. *Annual return, payment of tax.* (1) On or before March 20 after the end of the tax year each taxpayer shall make a return showing the gross proceeds of sales or gross income, and compute the amount of tax chargeable against him in accordance with the provisions of this Act and deduct the amount of monthly payments (as hereinbefore provided), and transmit with his report a remittance in the form required by section 12 of this Act covering the residue of the tax chargeable against him to the office of the appropriate territorial divisional tax assessor hereinafter designated; such return shall be verified by the oath of the taxpayer, if made by an individual, or by oath of the president, vice-president, secretary, or treasurer, of a corporation, if made on behalf of a corporation. If made on behalf of a partnership, firm, society, unincorporated association, group, hui, joint adventure, joint stock company, corporation, trust estate, decedent's estate, trust or other entity, any individual delegated by such partnership, firm,

society, unincorporated association, joint adventure, group, hui, joint stock company, corporation, trust estate, decedent's estate, trust or other entity shall make the oath on behalf of the taxpayer. If for any reason it is not practicable for the individual taxpayer to make the oath, the same may be made by any duly authorized agent. The tax commissioner, for good cause shown, may extend the time for making such return on the application of any taxpayer and grant such reasonable additional time within which to make the same as may, by him, be deemed advisable.

(2) All monthly and annual returns shall be transmitted respectively to the office of the territorial divisional tax assessor of the taxation division in which the privilege upon which the tax accrued is exercised; provided, however, that where such privilege is exercised in more than one taxation division the said returns shall be transmitted to the office of the assessor of the first taxation division.

(3) *Consolidated reports; inter-related business.* When any taxpayer is engaged in two or more forms of business activity taxable under the provisions of this Act which are inter-related, or which are of like character, such taxpayer shall file a consolidated return covering all business activities, which are thus inter-related or of like character.

(4) The provisions of this section shall apply to every person registered or required to be registered under section 4 of this Act, provided, that while an application for exemption is pending before the tax

commissioner or if it be allowed no payment of tax need accompany the return. (L. 1935, c. 141, s. 6; am. L. 1941, c. 265, s. 4.)

Section 7. *Erroneous returns, disallowance of exemption, payment, refund.* (1) If any return made is erroneous, or is so deficient as not to disclose the full tax liability, or if the taxpayer, in his return, shall disclaim liability for the tax on any gross income or gross proceeds of sales liable to the tax, the tax commissioner shall correct such error or assess the proper amount of taxes. If such recomputation results in an additional tax liability, or if the commissioner proposes to assess any gross income or gross proceeds of sales by reason of the disallowance of an exemption, the commissioner shall first give notice to the taxpayer of the proposed assessment, and the taxpayer shall thereupon have an opportunity within thirty days to confer with the commissioner. After the expiration of thirty days from such notification the commissioner shall assess the gross income or gross proceeds of sales of the taxpayer or any portion thereof which he believes has not heretofore been assessed, and shall give notice to the taxpayer of the amount of the tax, and the amount thereof shall be due and payable on the twenty-first day after the date the notice was mailed, properly addressed to the taxpayer at his last known address or place of business. Provided, that no preliminary notice shall be necessary where the amount of the tax is calculated by the commissioner from gross income returned

by the taxpayer as subject to the tax (unless the taxpayer shall have claimed that the one-quarter ($\frac{1}{4}$) of one per cent rate is applicable and the commissioner shall have applied the one and one-quarter ($1\frac{1}{4}$) per cent rate); in such case the tax shall be due and payable on the tenth day after the date the statement was mailed.

(2) If the amount already paid exceeds that which should have been paid on the basis of the tax so recomputed, the excess so paid shall be immediately refunded to the taxpayer upon the requisition of the tax commissioner on the territorial auditor, who shall issue his warrant in the form prescribed by the Revised Laws of Hawaii 1935, section 594, on the territorial treasurer, which shall be payable out of the "gross income tax reserve fund" in the next succeeding paragraph hereof created. The taxpayer may, at his election, apply an overpayment credit to taxes subsequently accruing hereunder. All refunds and the details thereof, including the names of the persons receiving the refund and the amount refunded, shall be posted on a bulletin board which shall be maintained in a place accessible to the public in the office of the assessor of the taxation division in which the person receiving the refund made his returns.

(3) There is hereby appropriated from the general revenues of the Territory, not otherwise appropriated, the sum of ten thousand dollars (\$10,000.00) which shall be set aside as a special fund to be known as the "gross income tax reserve fund", the same to be subject to the warrants of the auditor of the Ter-

ritory upon the treasurer of the Territory, as in and by this Act provided.

(4) The tax commissioner in his discretion may from time to time deposit taxes collected by him under the provisions of this Act in the territorial treasury to the credit of the "gross income tax reserve fund" so that there shall be maintained at all times a fund of ten thousand dollars (\$10,000.00). (L. 1935, c. 141, s. 7; am. L. 1941, c. 265, s. 5.)

Section 8. *Failure to make return.* If any person shall fail, neglect or refuse to make a return, the commissioner may proceed as he deems best to obtain information on which to base the assessment of the tax. After procuring such information the commissioner shall proceed to assess the tax and shall notify the person assessed of the amount of the tax and penalty. Any assessment of tax by the tax commissioner made pursuant to the provisions of this section shall be final, and any tax so assessed shall be deemed to have been in default from the time when such tax should have been returned and paid. (L. 1935, c. 141, s. 8; R. L. 1935, s. 2025H; am. L. 1941, c. 265, s. 6.)

Section 8-A. *Audits, procedure, penalties.* (1) *Audit.* The commissioner or any duly appointed deputy tax commissioner, assessor, or deputy assessor, or a responsible person designated by the commissioner or by a deputy tax commissioner to act in the premises for the purpose of verification or audit of a return made by the taxpayer, or where there is reasonable ground to believe that any return made is so deficient

as not to form the basis of a satisfactory assessment of the tax, or for the purpose of making an assessment where no return has been made, is authorized and empowered to examine all account books, bank books, bank statements, records, vouchers, taxpayer's copies of federal tax returns, and any and all other documents and evidences having any relevancy to the determination of the gross income or gross proceeds of sales of any taxpayer as required to be returned under this Act and may summon or require the attendance of the person by or for whom the return (if any) has been made or whose tax is being assessed, and any employee of such person, and may summon or require the attendance of any person having knowledge in the premises, naming the time and place in the summons, and may require the production of any books, statements or other evidences open to his examination, and may take testimony in reference to any such matter relevant to the gross income or gross proceeds of sales of the taxpayer for the period under consideration, with power to require that the person so called and appearing shall be interrogated under oath and to administer such oath.

(2) *Additional taxes.* If the commissioner determines that any gross income or gross proceeds of sales liable to the tax have not been assessed he may assess the same as provided in sections 7 and 8 of this Act.

(3) *False swearing perjury.* Any individual knowingly giving false testimony under oath at any such hearing before the commissioner or other person au-

thorized to conduct such hearing under the provisions of this section shall be guilty of perjury and shall be punished as provided by law.

(4) *Refusal to obey summons or testify; penalty.* Any person refusing or neglecting to obey any summons issued by the commissioner or other person authorized to issue such summons under the provisions of this section, and any individual appearing and refusing to testify under oath, shall be guilty of a misdemeanor and on conviction thereof shall be punished by a fine of fifty dollars for the first offense and one hundred dollars for each succeeding offense. (L. 1935, c. 141, s. 8; am. L. 1941, c. 265, s. 7.)

Section 9. *Appeal; correction of assessment.* If any person having made the return and paid the tax for any month or any year as provided by this Act feels aggrieved by the assessment so made upon him by the tax commissioner, he may appeal from said assessment in the manner and within the time and upon giving notice in writing stating his grounds of appeal to the person specified in section 2045 of the Revised Laws of Hawaii 1935. Where final judgment is in favor of the taxpayer for the repayment to him in whole or in part of taxes paid and no appeal has been perfected therefrom, the auditor of the Territory shall, upon the presentation by the taxpayer to him of a certified copy of said final judgment, issue his warrant in payment of said judgment in the form prescribed by the Revised Laws of Hawaii 1935, section 594, on the territorial treasury which shall be payable

out of the "gross income tax reserve fund" in this Act created, provided, however, that where final judgment is in favor of the taxpayer for the redetermination of a monthly installment of tax and no appeal has been perfected therefrom the excess tax paid shall constitute an overpayment credit which shall be applied to taxes subsequently accruing, if any, and refunded to the extent of overpayment of the assessment for the year as herein elsewhere provided. (L. 1935, c. 141, s. 9; am. L. 1937, c. 202, s. 1.)

Section 10. *Tax year.* The assessment of taxes herein made and the returns required therefor shall be for the year ending on the thirty-first day of December. If the taxpayer, in exercising a privilege taxable under this Act, keeps his books reflecting the same on a basis other than the calendar year, he may, with the assent of the tax commissioner, make his annual returns and pay taxes for the year covering his accounting period, as shown by the method of keeping his books.

Section 11. *Tax cumulative.* The tax imposed by this Act shall be in addition to all other licenses and taxes levied by law as a condition precedent to engaging in any business, trade or calling. A person exercising a privilege taxable under this Act, subject to the payment of all licenses and charges which are conditions precedent to exercising the privilege taxed, may exercise the privilege for the current tax year upon the condition that he shall pay the tax accruing under this Act.

Section 12. *Remittances.* All remittances of taxes imposed by this Act shall be made to the tax assessor to whose office the return was transmitted by money, bank draft, check, cashier's check, money order, or certificate of deposit, who shall issue his receipts therefor to the taxpayer and shall pay the moneys into the territorial treasury as a territorial realization, to be kept and accounted for as provided by law.

Section 13. *Tax debt due Territory; lien; bulk sales; penalty for failure to pay.* (1) A tax due and unpaid under this Act shall be a debt due the Territory and shall be a lien upon the property used in the business or occupation upon which it is imposed. The lien shall have the same priority as the lien of territorial real property taxes.

(2) In any case of the sale in bulk of the whole, or a large part of a stock of merchandise and fixtures, or mechandise, or fixtures, or other assets of a business, otherwise than in the ordinary course of trade, and in the regular and usual prosecution of the seller's business, the seller shall make a written and verified report of such bulk sale to the tax commissioner not later than ten days after the possession, or the control, or the title of the property, or any part thereof, has passed to the purchaser, which report shall contain the name and address of the purchaser, a brief description of the property sold and the purchase price, the date when such sale is to be or was consummated, and such other facts as the tax commissioner may require. The purchaser may make such report for the seller. The purchaser of such property shall with-

hold payment of the purchase price until the receipt of a certificate from the tax commissioner to the effect that all taxes, penalties and interest levied or accrued under this Act against the seller, or constituting a lien upon such property, have been paid, which certificate shall show on its face that the tax commissioner has had notice of the bulk sale, and shall also show the names of the seller and purchaser, a brief description of the property sold, and the date of consummation of the sale, together with such other information as the tax commissioner shall prescribe. If the required report of the bulk sale is not made, or if the said taxes, penalties and interest shall not be paid within twenty days after the possession, or the control, or the title of the property, or any part thereof, has passed to the purchaser, or within such further time as the tax commissioner may allow, the purchaser shall be personally liable to pay to the Territory the amount of all taxes, penalties and interest levied or accrued under this Act against the seller or constituting a lien upon such property, together with penalties and interest thereafter accruing, not exceeding, however, the amount of the purchase price, provided, that the issuance of a certificate in the prescribed form shall be a complete defense to such liability of the purchaser. In any case of such liability upon the part of the purchaser a written report thereof shall be made by the purchaser upon the next due date for the payment of gross income taxes. For the purposes of this subsection the "purchase price" shall include money, or the value of any consideration other than money.

Failure to make any report required by this subsection shall constitute a misdemeanor punishable by a fine of not more than one hundred dollars (\$100.00). In addition, penalties and interest shall apply to such delinquent taxes if not paid within twenty days after the possession, or the control, or the title of the property, or any part thereof, has passed to the purchaser, or within such further time as the tax commissioner may allow, whether or not an assessment of the tax has been made or notice of the delinquency given. The purchaser shall have his remedy against the seller for the amount of taxes, penalties or interest paid by him.

(3) A penalty of five per cent of the tax shall be added for any default for thirty days or less and for each succeeding calendar month or fraction thereof elapsing before payment, there shall be added interest of one per cent, which penalty and interest shall be and become a part of the tax and be collected as a part thereof. The additional one per cent interest shall not apply until a ten-day notice of delinquency shall have been sent to the taxpayer. (L. 1935, c. 141, s. 13; R. L. 1935, s. 2025M; am. L. 1939, c. 213, s. 3; am. L. 1941, c. 265, s. 8.)

Section 14. *Collection by suit; injunction.* The tax commissioner may, by himself, or a duly appointed deputy commissioner or assessor, or tax collector, collect taxes due and unpaid under this Act, together with all accrued penalties, by action in assumpsit or other appropriate proceedings in the circuit court of the judicial circuit in which the privilege taxed has been exercised. After delinquency shall have continued

for sixty days, or if any person lawfully required so to do under this Act shall fail to apply for and secure a license as provided by this Act for a period of sixty days after the first date when he was required under this Act to secure the same, the tax commissioner may proceed, by himself or a deputy commissioner or assessor, in the circuit court of the judicial circuit in which the privilege taxed or taxable has been exercised, to obtain an injunction restraining the further exercise of the privilege until full payment shall have been made of all taxes and penalties and interest due under this Act, or until such license is secured, or both, as the circumstances of the case may require.

Section 15. *District magistrates; concurrent civil jurisdiction in tax collections.* Except as otherwise specifically provided by this Act, the several district magistrates shall have concurrent jurisdiction with the circuit courts to hear and determine all civil actions at law in assumpsit for the collection and enforcement of collection and payment of all taxes assessed hereunder, irrespective of the amount claimed.

Section 16. *Prerequisite for final settlement of contracts with the Territory or subdivisions thereof.* All territorial, county and city and county officers and agents making contracts on behalf of the Territory of Hawaii or any political subdivision thereof shall withhold payment in the final settlement of such contracts until the receipt of a certificate from the tax commissioner to the effect that all taxes levied or accrued under this Act against the contractor with respect to such contracts have been paid.

Section 17. *Collection of tax.* The tax commissioner for the more effective collection of the tax may file in the office of the registrar of conveyances of the Territory of Hawaii, at Honolulu, a certified copy of an assessment or assessments of taxes under this Act. A certificate so filed shall be recorded in a book provided for the purpose and thereafter shall constitute a lien upon all lands of the taxpayer located in the Territory of Hawaii as against all parties whose interest arose after such recordation. Upon payment of taxes delinquent under this Act the lien of which shall have been recorded the tax commissioner shall certify in duplicate the fact and amount of payment, and the balance due, if any, and shall forward the certificates, one to the taxpayer and one to the said registrar. The registrar shall record the certificate in the book in which releases are recorded, without payment of any additional fee. From the date that such a certificate is admitted to record the land of the taxpayer in the Territory of Hawaii shall be free from any lien for taxes under this Act accrued to the date that the certificate was issued. (L. 1935, c. 141, s. 17; am. L. 1941, c. 265, s. 9.)

Section 18. *Collection by distraint.* The tax commissioner may distraint upon any goods, chattels or intangibles represented by negotiable evidences of indebtedness, of any taxpayer delinquent under this Act for the amount of all taxes and penalties accrued and unpaid hereunder. The commissioner may require the assistance of the high sheriff or the sheriff of any county or city and county in which such sheriff is an

officer. A sheriff so collecting taxes due hereunder shall be entitled to compensation in the amount of all penalties collected over and above the principal amount of the tax due, but in no case shall such compensation exceed twenty-five dollars (\$25.00). All taxes and penalties so collected shall be reported within ten days after collection to the tax commissioner, who shall prescribe by general regulation the manner of remittance of such funds and of allowing the collecting officer the compensation due him under this section. (L. 1935, c. 141, s. 18; am. L. 1941, c. 265, s. 10.)

Section 19. *Offenses; penalties.* It shall be unlawful for any person to refuse to make the return provided to be made in section 6 of this Act; or to make any false or fraudulent return or false statement in any return, with intent to defraud the Territory or to evade the payment of the tax, or any part thereof, imposed by this Act; or for any person to aid or abet another in any attempt to evade the payment of the tax or any part thereof, imposed by this Act; or for the president, vice-president, secretary or treasurer of any corporation to make or permit to be made for any corporation or association any false return, or any false statement in any return required by this Act, with the intention to evade the payment of any tax hereunder. Any person violating any of the provisions of this section shall be guilty of a misdemeanor, and, on conviction thereof, shall be fined not more than one thousand dollars (\$1,000.00) or imprisoned for a period not exceeding one year, or punished by both fine and imprisonment, at the discretion of the court, with-

in the limitation aforesaid. In addition to the foregoing penalties, any person who shall knowingly swear to or verify any false or fraudulent return, or any return containing any false or fraudulent statement, with the intent aforesaid, shall be guilty of the offense of perjury, and, on conviction thereof, shall be punished in the manner provided by law. Any corporation for which a false return, or a return containing a false statement, as aforesaid, shall be made, shall be guilty of a misdemeanor and shall be punished by a fine of not more than one thousand dollars (\$1,000.00).

Section 20. *Administration and enforcement by tax commissioner.* (1) The administration of this Act is vested in and shall be exercised by the tax commissioner who shall prescribe forms and reasonable rules of procedure in conformity with this Act for the making of returns and for the ascertainment, assessment and collection of the taxes imposed hereunder. Such forms and rules when prescribed by the tax commissioner and printed and published in the manner provided by law shall have the force and effect of law. The enforcement of any of the provisions of this Act in any of the courts of the Territory shall be under the exclusive jurisdiction of the tax commissioner, who shall require the assistance of the attorney general of the Territory, and the city and county attorney and the respective county attorneys of the city and county, or of the counties where suit is brought; but said attorneys shall receive no fees or compensation for services rendered in enforcing this Act in addition to the respective salaries paid by law to such attorneys.

(2) The tax commissioner of the territory and the several deputy tax commissioners, divisional assessors, assistant assessors and other assistants, and tax collectors appointed by the tax commissioner, shall have, in addition to all of the duties and powers herein respectively prescribed or granted, all the duties and powers respectively prescribed or granted by the existing or future tax laws of the Territory so far as the same may be applicable to the administration of the within Act and are not contrary to the express provisions hereof.

Section 21. *Licenses; penalty for failure to secure.* Any person who shall have a gross income or gross proceeds of sales upon which a privilege tax is imposed by this Act, as a condition precedent to engaging or continuing in such business, shall in writing apply for and obtain from the tax commissioner, upon payment of the sum of one dollar (\$1.00) a license to engage in and to conduct such business for the current tax year, upon condition that he shall pay the taxes accruing to the Territory under the provisions of this Act, and he shall thereby be duly licensed to engage in and conduct such business. Said license shall be renewed annually and shall expire on the thirty-first day of December next succeeding the date of its issuance. Licenses and applications therefor shall be in such form as the commissioner shall prescribe, except that where the licensee is engaged in two or more forms of business of different classification, the license shall so state on its face. Any person who may lawfully be required by the Territory, and who is required

by this Act, to secure a license as a condition precedent to engaging or continuing in any business subject to taxation under this Act, who shall engage or continue in such business without securing such license in conformity with this Act, shall be guilty of a misdemeanor; and any director, president, secretary or treasurer of a corporation who permits, aids or abets such corporation to engage or continue in business without securing a license in conformity with this Act, shall likewise be guilty of a misdemeanor; the penalty for such misdemeanor shall be that prescribed by section 19 for individuals, corporations or officers of corporations, as the case may be, for violation of said section 19.

Section 22. *Records to be kept; examination.* It shall be the duty of every taxpayer to keep in the English language and preserve for a period of five years suitable records of gross proceeds of sales and gross income, and such other books, records of account and invoices as may be required by the commissioner, and all such books, records and invoices shall be open for examination at any time by the commissioner, or his duly authorized deputy, or by the divisional assessor (or his deputy) in whose office the return, returns and reports of the taxpayer are, or should be, filed under the provisions of this Act. Any person violating the provisions of this section shall be guilty of a misdemeanor; and any director, president, secretary or treasurer of a corporation who permits, aids or abets such corporation to violate the provisions of this section shall likewise be guilty of a misdemeanor; the

penalty for such misdemeanor shall be that prescribed by section 19 for individuals, corporations or officers of corporations, as the case may be, for violation of said section 19. (L. 1935, c. 141, s. 22; am. L. 1937, c. 202, s. 2; am. L. 1943, c. 140, s. 1.)

Section 22-A. *Limitation period for assessment, levy, collection, or refunding of taxes.* (1) *General rule.* The amount of excise taxes imposed by this Act shall be assessed or levied within five years after the annual return was filed and no proceeding in court without assessment for the collection of any such taxes shall be begun after the expiration of such period.

(2) *Exceptions; fraudulent return or no return.* In the case of a false or fraudulent return with intent to evade tax, or of a failure to file the annual return, the tax may be assessed or levied at any time; provided, however, that in the case of a return claimed to be false or fraudulent with intent to evade tax, the determination as to such claim must first be made by a judge of the circuit court as provided in section 2050, paragraph 2, of the Revised Laws of Hawaii 1935, which shall apply to the taxes imposed by this Act.

(3) *Extension by agreement.* Where, before the expiration of the period prescribed in subsection (1) of this section, both the tax commissioner and the taxpayer have consented in writing to the assessment or levy of the tax after the date fixed by said subsection (1), the tax may be assessed or levied at any time prior to the expiration of the period agreed upon. The period so agreed upon may be extended by subsequent

agreements in writing made before the expiration of the period previously agreed upon.

(4) *Refunds.* No credit or refund shall be allowed more than five years after the annual return was filed, or in any case of payment of tax without the filing of an annual return, more than five years after such payment of tax, unless a claim for such credit or refund was filed within such period. Provided, that such limitation shall not apply to a credit or refund pursuant to an appeal, provided for by section 9. (L. 1935, c. 141, s. 22; am. L. 1943, c. 140, s. 2.)

Section 23. *Unfair competition; penalty.* No taxpayer shall advertise or hold out to the public in any manner, directly or indirectly, that the tax hereby imposed upon him is not considered as an element in the price to the purchaser. Any person violating the provisions of this section shall be guilty of a misdemeanor and upon the conviction thereof shall be punished by a fine of not more than fifty dollars (\$50.00) for each offense.

Section 24. *Constitutionality.* If any section, subsection, sentence, clause or phrase of this Act is for any reason held to be unconstitutional or invalid, such decision shall not affect the validity of the remaining portions of this Act. The legislature hereby declares that it would have approved this Act and each section, subsection, sentence, clause and phrase thereof, irrespective of the fact that any one or more of the sections, subsections, sentences, clauses or phrases be declared unconstitutional or invalid. If the application of any provision of this Act to any person or circum-

stances is held invalid, the application of such provision to other persons or circumstances shall not be affected thereby.

Section 25. *Effective time of Act.* This Act shall take effect on July 1, 1935; provided, however, that, for the exercise, during the period from July 1 to December 31, 1935, of any of the privileges taxed by this Act, every person shall apply for and secure, on or before July 31, 1935, in the manner and under the conditions provided by section 21, a license, and shall pay therefor the sum of one dollar (\$1.00); and provided, further, that this Act shall only become effective in the event Senate Bills 24, 40, 145 and 215 become law.

No. 11,688

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

THOMAS H. BRODHEAD, doing business
as T. H. Brodhead Co.,

Appellant,

vs.

WILLIAM BORTHWICK, Tax Commis-
sioner and Tax Collector of the Ter-
ritory of Hawaii,

Appellee.

Upon Appeal from the Supreme Court for the
Territory of Hawaii.

REPLY BRIEF FOR APPELLANT.

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sioner and Tax Collector of the Ter-
ritory of Hawaii,

Appellee.

Upon Appeal from the Supreme Court for the
Territory of Hawaii.

REPLY BRIEF FOR APPELLANT.

ARGUMENT.

- A. THE TERRITORY OF HAWAII CANNOT LAWFULLY IMPOSE A TAX ON THE GROSS RECEIPTS FROM SALES TO THE UNITED STATES OR ITS AGENCIES OR INSTRUMENTALITIES.
1. The Territory of Hawaii is not a sovereign government with inherent power to impose taxes, but derives its power to tax from the United States.
 2. Congress has never delegated to the Territory of Hawaii power to tax the United States or its agencies or instrumentalities.

Appellee contends that the Territory of Hawaii was created as a sovereign government with full power to

impose taxes and that the Territorial power to tax the United States and its agencies and instrumentalities is as great as and no greater than the powers of the states with respect to such taxation. *Kawananakoa v. Polyblank*,¹ which is cited as holding that the Territory of Hawaii was created by Congress as a sovereign government, falls far short of such holding. It merely holds that the doctrine that a sovereign is exempt from suit was applicable in a mortgage foreclosure suit against the Territory of Hawaii on the ground that the doctrine is not confined to powers that are sovereign in the full sense of juridical theory, but naturally is extended to those that in actual administration originate and change at will the laws of contract and property from which persons within its jurisdiction derive their rights. Since the Organic Act placed the classification and control of the body of private rights in the Legislature of the Territory of Hawaii, the fountainhead from which such rights flow is the Territory and, consequently, as between it and its citizens, the Territory is supreme.

In support of the claim that the Territory has the full taxing power which Congress, itself, could have exercised, the Appellee cites *Yerian v. Territory of Hawaii*,² *Rivera v. Buscaglia*,³ and *Haavik v. Alaska Packers Asso.*⁴

¹205 U.S. 349, 51 L. ed. 834 (1907).

²130 F.2d 786 (C.C.A. 9, 1942).

³146 F.2d 461 (C.C.A. 1, 1944).

⁴263 U.S. 510, 68 L. ed. 414 (1924).

In the *Yerian*² case, *supra*, there was involved not a tax on the United States or its agencies or instrumentalities, but a tax on the compensation of employees of instrumentalities of the United States which the court held were not exempted from the tax and could have been taxed even if Congress had not consented. Actually, however, Congress has consented to the taxation of such salaries under Section 4 of the *Public Salaries Tax Act of 1939*,⁵ provided that there is no discrimination against such employees because of the source of their compensation. In *Rivera v. Buscaglia*,⁶ *supra*, the court stated that the question of whether Puerto Rico may tax the salaries of a certain employee of the federal government depends upon whether Congress has given consent, which is distinct from the question of reciprocal immunity from tax as between the federal government and the states of a union to be derived from the general scheme of the Constitution of the United States. The court analysed the history of the taxing Act and found that there was an implication that Congress intended to include the salaries of federal employees as subject to tax, and in any event held that consent had been specifically given to the tax under the *Public Salaries Tax Act of 1939*,⁷ *supra*.

The *Haavik*⁸ case, *supra*, in holding that Alaska was given the right to tax to the full extent that Congress could, did not go so far as to give the territory the

⁵(5 U.S.C.A., Section 84(a)).

⁶146 F.2d 461 (C.C.A. 1, 1944).

⁷(5 U.S.C.A., Section 84(a)).

⁸263 U.S. 510, 68 L. ed. 414 (1924).

right to tax the United States or agencies or instrumentalities of the United States without its express consent.

The Congress has never delegated to the Territory of Hawaii power to tax the United States or its agencies or instrumentalities. *Domenech v. National City Bank*,⁹ *Posadas v. National City Bank*,¹⁰ *Puerto Rico v. Shell Co.*,¹¹ *Yerian v. Territory of Hawaii*,¹² *supra*.

The statement of this Court in the *Yerian*¹² case, *supra*, does not go as far as Appellee's statement " * * that the overruling of the doctrine of the tax immunity of those dealing with the federal government is as effective in the Territory of Hawaii as elsewhere."¹³ A continuation of the quotation of Appellee would go on to this Court's statement that a territory cannot any more than a state tax the federal government or its agencies or instrumentalities without the consent of Congress. Summarized, the conclusion would seem to be that neither a state nor a territory can tax the United States or instrumentalities thereof; that a state, by reason of its inherent sovereignty is limited by construction of the Constitution so that it cannot interfere with the activities of the United States in the exercise of its sovereign rights; that because of the necessity for the two sovereigns to coexist together, a certain leeway is permitted the

⁹294 U.S. 199, 79 L. ed. 857, 861 (1935).

¹⁰296 U.S. 497, 80 L. ed. 351, 354 (1936).

¹¹302 U.S. 253, 82 L. ed. 235, 247 (1937).

¹²130 F.2d 786 (C.C.A. 9, 1942).

¹³Brief for Appellee, p. 11.

state although some economic burden may fall on the federal government.

In the case of a territory, however, the territory may only burden the activities of the federal government to the extent provided by Congress itself, and there is not the same reason for permitting the burdening of the federal government by a territory as exists in the case of a state.

The *Yerian*¹⁴ case, *supra*, was intended to go no further than *Talbott v. Silver Bow County Commissioners*¹⁵ which construed a consent by Congress for states to tax national banks to include territories on the ground that the statute meant to include organized political societies with established governments, and not merely state as that term is used in the Constitution. The *Yerian*¹⁴ case, *supra*, does not go to the length of placing states and territories on the same basis in so far as their respective powers to impose taxes that may burden the United States are concerned. It should be noted that in the *Yerian*¹⁶ case, *supra*, this Court stated that there was not involved a tax on an instrumentality of the United States, but merely a tax on the compensation of employees of the United States. Appellee makes the point,¹⁷ which was conceded, that Congress may, by specific grant, give to territories taxing power denied to a state, and cites in support thereof *Inter-Island Steam Nav. Co. v.*

¹⁴130 F.2d 786 (C.C.A. 9, 1942).

¹⁵139 U.S. 438, 35 L. ed. 210 (1891).

¹⁶130 F.2d 786 (C.C.A. 9, 1942).

¹⁷Brief for Appellee, footnote p. 11.

Hawaii,¹⁸ and *Buscaglia v. Ballester*.¹⁹ These cases make clear the validity of Appellant's contention that the taxing power of the Territory is altogether different from the taxing powers of a state, being derived from Congress.

As between the United States and the creature it creates, there is no question but that the tax or the burden on the sovereign is only that which the sovereign permits. In the case of a state, the taxing power is inherent because the state is a sovereign power limited only by what has been granted to the federal government by the Constitution. A state tax, subject to certain limitations, may impose a burden on the federal government, but still, because of the necessity of the two sovereign powers coexisting together under our constitutional system, such a tax is tolerated.

Appellee cites²⁰ a number of reasons which it claims overcome the contention in the opening brief²¹ to the effect that the Organic Act is to be interpreted in the right of its meaning and intent when Congress adopted it. It is our contention that the argument of Appellee in this regard is specious.

It should be noted that in the *Yerian*²² case, *supra*, and *Rivera v. Buscaglia*,²³ *supra*, Congress has consented to the taxes there in question; that although the

¹⁸305 U.S. 306, 83 L. ed. 189 (1938).

¹⁹162 F.2d 805 (C.C.A. 1, 1947).

²⁰Brief for Appellee, pp. 12 to 14, incl.

²¹Opening brief, pp. 23 to 25, incl., and 27.

²²130 F.2d 786 (C.C.A. 9, 1942).

²³146 F.2d 461 (C.C.A. 1, 1944).

*Panhandle Oil Co. v. Mississippi ex rel. Knox*²⁴ case was decided in 1928, the doctrine on which it was bot-tomed did not originate in 1928, but went back to *McCulloch v. The State of Maryland, et al.*;²⁵ that there is no parallel between the grant of taxing power by a state to a municipality and a grant of taxing power by Congress to a territory. All the state tax cases cited go to the construction by the states of their own Acts, If, by reason of a changed construction of an Act it is judicially determined that a municipality has power to tax although previously it had been held otherwise, such power to tax as so determined has always existed subject to the state courts' own deter-mination of whether the statute or the ordinance or the constitution intended the tax power to be dele-gated. In the case of the Territory, it becomes a question of what the power of the Territory itself was, in which case it is necessary to go back to the intent of Congress in the enactment of the Organic Act from which the Territory derives its power. It is Appellant's contention that, by reason of the inherent difference in the fundamental nature of states and territories, the cases relating to the immunity of the federal government from taxation by the states are not authority in interpreting the immunity of the federal government from taxation or the imposition of burdens by the Territory.

²⁴277 U.S. 218, 72 L. ed. 857 (1928).

²⁵17 U.S. (Wheat. 4) 316, 4 L. ed. 579 (1819).

3. A statute which includes the gross receipts from sales to the United States and its agencies and instrumentalities, within the measure of the tax, is a tax on the United States.
4. The *Panhandle*²⁶ case, *supra*, has not been overruled in so far as the holding that a tax on sales to the United States is unconstitutional.

The case of *Wilson v. Cook*²⁷ is said to put at rest the remaining doubt as to the *Panhandle*²⁶ line of cases having been overruled.²⁸ This case did not involve a sale to the United States, but involved a contract for the purchase and severance of timber on national forest reserves. As stated by Appellee,²⁹ the court held that the Supreme Court of Arkansas was right in holding, “* * * that plaintiffs, who are taxed by the state on *their activities in severing lumber from Government lands*³⁰ under contract with the Government, cannot claim the benefit of the implied constitutional immunity of the Federal Government from taxation by the state.”³¹ Obviously this was a tax on activities of the plaintiffs under a contract with the United States which the court held was not a tax upon the government. Again, this is another case in which the claim to immunity depends on the claimed economic burden on the United States, which, while more direct than in the *James v. Dravo Contracting Co.*³² and *Alabama v. King & Boozer*³³ cases, is still not as direct

²⁶277 U.S. 218, 72 L. ed. 857 (1928).

²⁷327 U.S. 474, 90 L. ed. 793 (1946).

²⁸Brief for Appellee, p. 19.

²⁹Brief for Appellee, p. 20.

³⁰Emphasis supplied.

³¹327 U.S. 474, 483, 90 L. ed. 793, 800.

³²302 U.S. 134, 82 L. ed. 155 (1937).

³³314 U.S. 1, 86 L. ed. 3 (1941).

as in the case of sales to the United States here in question.

With respect to the cases cited by Appellee on which Appellee relies,³⁴ it should be noted that none of the federal cases cited relate to sales to the United States. *James v. Dravo Contracting Co.*,³⁵ *supra*, involved a tax on a contractor of the proceeds of his contract with the United States. *Western Lithograph Co. v. State Board of Equalization*³⁶ was based on the holding of the California court, at page 737, that the tax is not on the sale, but, rather, is a tax in the same category as property and excise taxes payable by an independent contractor engaged in the business of retail sales. It is a tax computed on the gross receipts from the conduct of the business of the retail merchant. The effect of this holding was substantially nullified in *Richfield Oil Corp. v. State Board of Eq.*³⁷ where the Supreme Court held that the designation of the tax was immaterial and that the real effect of the tax must be looked into.

The *Federal Land Bank of St. Paul v. De Rochford*³⁸ case states (without the benefit of Supreme Court approval) that the *Panhandle*³⁹ case, *supra*, has been overruled.

³⁴Brief for Appellee, pp. 22 to 27, incl.

³⁵302 U.S. 134, 82 L. ed. 155 (1937).

³⁶78 P.2d 731, 737 (1938).

³⁷329 U.S. 69, 91 L. ed. (Adv. Sheets) 123 (1946).

³⁸287 N.W. 522 (1939).

³⁹277 U.S. 218, 72 L. ed. 857 (1928).

*Compress of Union v. Stone*⁴⁰ involved a tax on the proceeds of services where sales to the United States were specifically exempted under the statute and, obviously, has no application.

*United States v. Lee*⁴¹ is similar to *Western Lithograph*,³⁶ *supra*, and its effect is nullified by the *Richfield Oil*³⁷ case, *supra*.

*Smith v. Davis*⁴² relates to an *ad valorem* tax which would seem to be irrelevant.

*Carnegie-Illinois Steel Corporation v. Alderson*⁴³ involved not sales to the United States, but, rather, a lump-sum contract for the manufacture of armor plate and deck plate used in the construction of warships, and is no different than the *Dravo*⁴⁴ case, *supra*.

*Reconstruction Finance Corp. v. Beaver County*⁴⁵ seems to lend no light to the questions in issue.

*Sanders v. Oklahoma Tax Commission*⁴⁶ is no different than the *King & Boozer*⁴⁷ case, *supra*.

*Salt Lake County v. Kennecott Copper Corporation*⁴⁸ involved an *ad valorem* tax and seems to have no application to the present case.

In addition, it should be noted that it is only if the tax is nondiscriminatory in so far as the federal

⁴⁰193 So. 329 (1940).

⁴¹13 So.2d 919 (1943).

⁴²323 U.S. 111, 89 L. ed. 107 (1944).

⁴³34 S.E.2d 737 (1945).

⁴⁴302 U.S. 134, 82 L. ed. 155 (1937).

⁴⁵328 U.S. 204, 90 L. ed. 851 (1946).

⁴⁶169 P.2d 748 (1946).

⁴⁷314 U.S. 1, 86 L. ed. 3 (1941).

⁴⁸163 F.2d 484 (C.C.A. 10, 1947).

government or its agencies are concerned that it may be, in any event, sustained.⁴⁹ If, for the reasons set forth in Section B hereof, it is held that the tax imposed by the Statute in question discriminates against the United States, then the act is unconstitutional *in toto*.

B. THE TERRITORY OF HAWAII CANNOT LAWFULLY IMPOSE A TAX AT A HIGHER RATE WITH RESPECT TO SALES TO POST EXCHANGES THAN WITH RESPECT TO SALES TO OTHER RETAIL MERCHANTS FOR RESALE.

There is nothing in the Statute to support the interpretation of the Supreme Court of the Territory of Hawaii that the statute makes any classification based on whether or not a second taxable activity occurs. As a matter of fact, under the scheme of the statute, it is quite reasonable to suppose, and it is possible that as many as four or five taxes may be laid upon sales of the same goods. The vice of the determination of the Supreme Court is that it has attempted to classify all activities of the federal government in the same class, regardless of the purpose for which various agencies of the United States may purchase the goods, the sale of which is subject to tax, and in effect did classify the government as "all other purchasers" regardless of whether the purchases were for resale or not.

The evidence of the Deputy Tax Commissioner in charge of gross income taxation is completely disre-

⁴⁹Opening brief, p. 43.

garded and the prior history of the collection of the tax is altogether omitted from the consideration of the court.

As testified by Mr. Westly, prior to January 1, 1942, the only tax on sales to the United States which the Territory sought to collect from the Statute were those to the post exchanges and ships' service stores at $\frac{1}{4}$ of 1%.⁵⁰ Beginning January 1, 1942, the tax on sales to post exchanges was increased to 1½%, and all sales to the United States were taxed at the same rate. The increase in tax was made because it was determined that post exchanges were not required to have a license because they were instrumentalities of the United States.⁵¹

From the evidence it was apparent that, as construed by the Tax Commissioner, post exchanges were originally treated as retail merchants purchasing for purposes of resale and, when it was to the advantage of the Territory, a wholesale tax was collected from sellers to post exchanges at a time when all other sales to the United States were deemed to be exempt from tax. When it was determined, at least to the satisfaction of the Territory, that the Territory could tax sales to the United States, it chose not to distinguish the two kinds of sales, but to treat all sales to the United States as subject to tax, although it had always recognized sales to post exchanges as being properly taxable at the wholesale rate.

⁵⁰R. 155-6.

⁵¹R. 160-1.

The question is asked in Appellee's brief whether the Territory can, in a privilege tax act which taxes every sale, service or other activity, avoid the undue pyramiding of the tax by prescribing a lower rate where a second taxable activity is to follow, and, if it does, must it segregate and give consideration to an activity of the United States which, for taxation purposes, it is required to disregard.⁵² While there cannot be much question that the avoidance of undue pyramiding of a tax is a valid purpose of classification, as stated above, that is not the purpose of the Act nor is it in any way accomplished by the Act. The same Legislature which enacted the tax Act here in question enacted a Use and/or Consumption Tax Act⁵³ under which there was exempted sales which were subject to tax under the Gross Income Tax Act. The language of that Act is plain and clear, and it seems unreasonable to suppose that the Legislature, if it had intended to exempt or give a lower rate of tax to sales previously taxed, could have stated its intention in clear and plain language.

In the General Excise Tax Act itself there are several provisions which indicate that the Legislature knew how to state an exemption or how to prevent double taxation if that was its purpose.⁵⁴ The absence of such language in the Act clearly indicates that there was no intention to prevent a so-called "pyramiding of tax." On the other hand, it is much more reason-

⁵²Brief for Appellee, p. 35.

⁵³Act 160, Session Laws of Hawaii, 1935.

⁵⁴See, for example, Brief for Appellee, App. Sec. 2, C(2), D(2), pp. 12, 14, incl.

able to suppose that the Legislature classified wholesalers as such and imposed a smaller tax with regard to their sales because wholesalers generally deal in larger quantities and have a greater volume of sales with a smaller mark-up and thus are not able to pay as high a tax as retailers whose mark-up is higher and whose turnover is much smaller.

The Appellee contends⁵⁵ that the Supreme Court balanced the $11\frac{1}{2}\%$ tax paid upon sales to the United States, the $\frac{1}{4}$ of 1% on the sale to licensed merchants, plus the $11\frac{1}{2}\%$ added before the goods reached the consumer, and found a fair balance. The actual fact, however, is that this tax, collected from the seller on sales to the post exchanges, was collected at the higher rate because it was determined that the Territory could not collect on account of the sales of the post exchanges.

In an opinion of the Attorney General to Honorable William Borthwick, January 8, 1945,⁵⁶ it was stated that since the Statute does not make any difference in a service business because of the intrusion of a middle-man, certain transactions were taxable at the retail rate; that it was only in sales that different rates were applicable. In the opinion there is no suggestion of any purpose of the law to prevent pyramiding, although each of the cases cited were cases in which relief should have been accorded if the statute had any such intention. For example, there was in question the case of a customer bringing a film to

⁵⁵Brief for Appellee, p. 37.

⁵⁶Hawaii Tax Service, P-H, Par. 23042.

a drugstore to have prints made therefrom. The drugstore sends the film to Kodak Hawaii to have the prints made. Kodak Hawaii makes the prints and sells them at wholesale prices to the drugstore which, in turn, resells them to the customer at retail prices. Held that Kodak Hawaii must pay a retail tax as must the drugstore. Another case⁵⁷ is where a customer requests a drugstore to develop a roll of film and make a clear negative. Kodak Hawaii does the work, charging wholesale prices, and, on resale, the drugstore makes a retail charge. Held both Kodak Hawaii and the drugstore are subject to tax at the retail rate.

The argument of Appellee, based on a composite tax structure to prove that the United States has suffered no harm by reason of the tax imposed on account of sales to post exchanges at reduced rates, is pure fancy. The case of *Tradesmens Nat. Bank v. Oklahoma Tax Com.*⁵⁸ in no way sanctions a so-called "composite tax structure". There, the court merely examined the practical question of whether a national bank was being discriminated against under an act of Congress which expressly permitted states to tax national banks at a rate no higher than other businesses. Under the express consent granted, it was necessary to determine whether, under different types of taxes, there was any discrimination against the national bank. In arguing that in the Territory of

⁵⁷Included in the same opinion (Hawaii Tax Service, P-H, Par. 23042).

⁵⁸309 U.S. 560, 84 L. ed. 947 (1940).

Hawaii the same procedure was followed, it is contended that there was a total of $11\frac{1}{2}\%$ added before goods reached the consumer through taxation of the sale to post exchanges, as against $13\frac{1}{4}\%$ where goods reached the consumer through other retail sources, Appellee attempts to make the composite tax structure the yardstick.

Such a test is, of course, one based upon indirect economic burden upon the United States, and is not a proper test in determining whether there has been discrimination against the United States or not. The true test of discrimination is a practical one, as set forth on pp. 56 to 59, inclusive, in the opening brief.

Wilson v. Cook,⁵⁹ *supra*, which is stated⁶⁰ to afford a decisive answer to Appellant's claim of discrimination, did not answer the question of discrimination at all. In the majority opinion, the court said that it was not determining, because it was not called on to determine " * * * whether plaintiffs could have successfully contested their liability in the state courts or here, if the contentions were properly raised, upon the ground that they would be unable to collect the tax from the Government, *either*⁶¹ because the provision purporting to allow such collection is inapplicable where the owner is the Government *or*⁶¹ if applicable, invalid, *or*⁶¹ on the ground that the tax, applied to them without recourse against the Govern-

⁵⁹327 U.S. 474, 90 L. ed. 793 (1946).

⁶⁰Brief for Appellee, p. 39.

⁶¹Emphasis supplied.

ment, would deny to them the equal protection of the laws.’’⁶²

The reference to the holding of the majority of the court that any claim of discrimination “* * * would lie under the equal protection clause, not the federal immunity doctrine * * *”,⁶³ is not borne out by the language of the court referred to above. The court pointed out, as noted above, that there were three alternative contentions that might have been made by the plaintiffs which were not made, and that, therefore, it did not pass on the question of discrimination. Further, in the dissenting opinion, it was stated that to treat the tax as applicable to the severer, and to treat the collection provisions from the government as inapplicable, would raise serious questions of discrimination which neither the state court nor *this court* has considered. Because the issue of discrimination was not raised since the plaintiffs had no way of knowing that the court, in its determination, would so construe the Act to make such a contention necessary, the dissenting Justice was of the opinion that the case should be remanded for a determination on the matter of the applicability of the collection provisions from the United States.

In so far as the *Kaiser Co. v. Reid*⁶⁴ and *S.R.A. Inc. v. Minnesota*⁶⁵ cases are cited with regard to discrimination, there seems to be no application to

⁶²327 U.S. 474, 485, 90 L. ed. 793.

⁶³Brief for Appellee, p. 40.

⁶⁴184 P.2d 879 (1947).

⁶⁵327 U.S. 558, 90 L. ed. 851 (1946).

the present case; the *Kaiser*⁶⁴ case, *supra*, being one of economic burden, and the *S.R.A.*⁶⁵ case, *supra*, involving an *ad valorem* property tax where, again, mere economic burden is involved.

The Appellee⁶⁶ states that the contention is that post exchanges are in competition with retail merchants for business.⁶⁷ This is an incorrect statement of the contention of the Appellant. The competition that is spoken of is on the right to purchase. The whole line of argument, in connection with the alleged factual discrimination, of the Appellee is false because it is based on a misconception of the argument of the Appellant, which is fully set forth in the opening brief.

CONCLUSION.

It is, therefore, respectfully submitted that:

I. The Territory of Hawaii cannot lawfully impose a tax on the gross receipts from sales to the United States or its agencies or instrumentalities.

(a) There is no proper analogy between the right of states and the right of territories to impose taxes on the United States or its agencies or instrumentalities, or their respective rights to impose burdens upon federal activities.

(b) In any event, it has not been finally held by the Supreme Court of the United States that a state may tax sales to the United States.

⁶⁶Brief for Appellee, pp. 46, 47.

⁶⁷Opening brief, p. 56.

II. The Territory of Hawaii cannot lawfully impose a tax at a higher rate with respect to sales to post exchanges than with respect to sellers to other retail merchants for resale.

(a) In determining whether a classification is proper, two separate taxes imposed on different taxpayers on account of different transactions cannot be considered together.

(b) The test of discrimination is a practical one, and it has been shown that the federal government is hindered in the purchase of merchandise in the Territory of Hawaii by reason of the higher tax upon sales to post exchanges than on sales to other persons for resale.

Dated, Honolulu, T. H.,

August 20, 1948.

URBAN E. WILD,

MILTON CADES,

By URBAN E. WILD,

His Attorney-in-Fact,

Attorneys for Appellant.

SMITH, WILD, BEEBE & CADES,

Of Counsel.

No. 11689

United States
Circuit Court of Appeals
For the Ninth Circuit

WESTERN UNION TELEGRAPH COMPANY,
a corporation,

Appellant,

vs.

HANSEN & ROWLAND CORPORATION,
a corporation,

Appellee.

Transcript of Record

Upon Appeal from the District Court of the United States
for the Western District of Washington,
Southern Division

FILED

AUG 2 1947





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WESTERN UNION TELEGRAPH COMPANY,
a corporation,

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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CHARLES T. PETERSON, ESQ.,

WENDELL W. DUNCAN, ESQ.,

Perkins Building,

Tacoma, Washington,

Attorneys for Appellees.

In the Superior Court of the State of Washington
in and for the County of Pierce

No. 99059

HANSEN & ROWLAND CORPORATION,
a corporation,

Plaintiff,

vs.

THE WESTERN UNION TELEGRAPH COM-
PANY, a corporation,

Defendant.

COMPLAINT

Comes now plaintiff and complaining of defendant says:

I.

Plaintiff is a corporation organized and existing under and by virtue of the laws of the State of Washington, and has paid its annual license fee for the year last past due.

II.

That defendant is a corporation organized and existing under and by virtue of the laws of the State of New York, and is and at the times herein mentioned was engaged in doing business in the State of Washington.

III.

That on the 2nd day of December, 1932, Premier Investment Company, a corporation, was the owner and in possession of Lot Four (4), Block One Thousand Three (1003), Map of New Tacoma, W. T., in Pierce County, Washington, commonly known as House No. 1007 Pacific Avenue in the City of Tacoma, Washington, and on said date entered into a lease in writing with defendant, The Western Union Telegraph Company, extending over a period of six years beginning on November 1st, 1932 and ending on the 31st day of October, 1938; that said lease contained among others the following provision:

“Unless either party hereto shall give to the other at least three months prior to the end of said term written notice of his or its desire and intent to terminate this lease at the end of said term, this lease shall continue upon the terms and conditions then in force for a further period of one year and so on from year to year until terminated by either party hereto giving to the other written notice at least three months prior to the expiration of the then current term of his or its desire and intent to terminate this lease at the end of said term.”

That during the month of May, 1938, said lease was extended by agreement in writing for a period of three years from the 1st day of November, 1938, by Western Union Realty Corporation, the then owner of said premises, and defendant; that the

provision above set forth in the original lease was by said agreement continued in force and thereafter on February 27th, 1941, was again extended by agreement in writing between Western Union Realty Corporation and defendant for the additional period of five years, beginning on the 1st day of November, 1941 and ending on the 1st day of November, 1946, and that said provision above set forth was by the said agreement in writing incorporated in said extension agreement and made a part thereof;

IV.

That subsequent to the making of said agreement last referred to and prior to July 24, 1946, plaintiff, Hansen & Rowland Corporation, acquired the legal title to and became the owner of said real property and premises, subject to the terms, provisions and conditions of said original lease made in 1932, and the written agreement last above referred to, extending the same, and is the owner of said real property and premises.

V.

That on July 24th, 1946, plaintiff made and delivered to defendant a notice in writing terminating defendant's right to occupy said premises from and after October 31st, 1946, a copy of which said notice is attached hereto, marked Exhibit "A" and made a part of this complaint by reference.

VI.

That on September 27th, 1946, plaintiff caused a notice in writing to be personally served on defend-

ant, notifying it to vacate and surrender up the premises to the owners thereof at the expiration of its tenancy on the 1st day of November, 1946, a copy of which said notice is attached hereto, marked Exhibit "B" and made a part of this complaint by reference.

VII.

That thereafter, on October 8th, 1946, defendant advised plaintiff orally that it desired to continue in possession of said premises after October 31st, 1946, following the expiration of its said lease as extended, whereupon plaintiff notified defendant in writing, that defendant would be permitted to remain in possession of said premises for a period not exceeding four months at a monthly rental of \$1500.00 per month, a copy of which said notice is attached hereto, marked Exhibit "C" and made a part of this complaint by reference.

VIII.

That on October 30th, 1946, defendant tendered to plaintiff as rental for said premises for the month of November, 1946, the sum of \$750.00, and notified plaintiff that it would not vacate and surrender up said premises, a copy of which said notice is attached hereto, marked Exhibit "D" and made a part of this complaint by reference.

IX.

That on November 2nd, 1946, plaintiff notified defendant in writing to pay the sum of \$1500.00 rent for said premises which became due and pay-

able on the 1st day of November, 1946, within three days after service of notice thereof, or in the alternative, to quit, vacate and surrender up the possession of said premises to plaintiff, the owner thereof, a copy of which said notice is attached hereto, marked Exhibit "E" and made a part of this complaint by reference; that defendant has failed, refused and neglected to vacate and surrender up the possession of said premises to plaintiff;

X.

That plaintiff is and for many years last past has been engaged in doing general insurance business, maintaining a general office at Tacoma, Washington, and among others, a branch office at Seattle, Washington, and at the present time and for some time past has employed a number of employees to carry on the different departments of its business, including a casualty department, and because of inability to obtain adequate office space within the City of Tacoma in which to carry on its business, it has been required and compelled to transfer the casualty department of its business from its general offices at Tacoma, Washington, to an office at Seattle, Washington, and compelled to incur unusual and unnecessary expense in that connection; that it could and would except for defendant's wrongful withholding and detaining possession of said premises maintain said casualty department at Tacoma, Washington, in the premises occupied by defendant and thereby save unnecessary expendi-

tures amounting to more than \$31.00 per day over and above the rental value of said premises, a statement of which said added unnecessary expenses is attached hereto, marked Exhibit "F" and made a part of this complaint by reference; that defendant long prior to its wrongful refusal to vacate and surrender up said premises was fully informed and knew that in case it wrongfully withheld and detained said premises from plaintiffs, that plaintiff would sustain such loss.

XI.

That in addition thereto, plaintiff has been damaged by defendant by failure to pay said rental at the rate of \$1500.00 per month in the amount of \$50.00 per day from and after November 1st, 1946, by reason of all of which plaintiff has sustained a loss of \$82.00 per day since November 1st, 1946, by reason of defendant's wrongful detention of said premises and will continue to sustain such amount of loss per day as long as defendant wrongfully withholds and detains possession of said premises.

Wherefore, plaintiff prays that it may have and recover possession of said premises from defendant, and that defendant be ousted therefrom, and that plaintiff have judgment against defendant for double the amount of the special damages, \$32.00 per day sustained by it from and including November 1st, 1946, until defendant surrenders up or is ousted from said premises, and for the further sum of \$100.00 per day, daily, being double the amount of the rent agreed to be paid for said premises from

and including November 1st, 1946, until defendant surrenders up said premises to plaintiff or is ousted therefrom, and that plaintiff have and recover its costs and disbursements herein.

PETERSON & DUNCAN,
Attorneys for Plaintiff.

State of Washington,
County of Pierce—ss.

Charles T. Peterson, being first duly sworn, on oath deposes and says:

That he is the attorney for Hansen & Rowland Corporation, a corporation, the plaintiff in the above entitled action, and makes this verification for and on its behalf; that all the material allegations set forth in the foregoing complaint are within his personal knowledge and that he has read the foregoing complaint, knows the contents thereof and the same is true as he verily believes.

CHARLES T. PETERSON.

Subscribed and sworn to before me this 9th day of November, 1946.

WENDELL W. DUNCAN,
Notary Public in and for the State of Washington,
residing at Tacoma.

[Endorsed]: Filed in County Clerk's Office,
Pierce County, Wash., Nov. 9, 1946. Josephine R.
Melton, Clerk. By C. I., Deputy.

EXHIBIT "F"

Unnecessary Expenses

3 additional stenographers at a combined salary of \$450.00 per month	\$450.00
Additional private telephone line from Seattle to Tacoma, per month	170.63
Temporary office equipment, Seattle	36.00
Salary and loss of time Casualty Department	150.00
Addition traveling expenses between Seattle and Tacoma because of transfer of Cas- ualty Department to Seattle, Washington	150.00
<hr/>	
Total per month	\$956.63

[Endorsed]: Filed in the United States District Court, Western District of Washington, Southern Division, Dec. 28, 1946. Millard P. Thomas, Clerk; By E. R., Deputy.

In the Superior Court of the State of Washington
in and for the County of Pierce

No. 99059

HANSEN & ROWLAND CORPORATION,
a corporation,

Plaintiff,

vs.

THE WESTERN UNION TELEGRAPH COM-
PANY, a corporation,

Defendant.

SUMMONS

The State of Washington to The Western Union
Telegraph Company, Defendant:

You Are Hereby Summoned to appear on the
18th day of November, A. D. 1946, and defend the
above entitled action in the court aforesaid, and
in case of your failure so to do, judgment will be
rendered against you according to the demand of
the complaint which has been filed with the Clerk
of said Court, a copy of which is herewith served
upon you.

PETERSON & DUNCAN,
Attorneys for Plaintiff.

[Endorsed]: Filed Nov. 9, 1946.

[Endorsed]: Filed in United States District
Court, Western District of Washington, Southern
Division, Dec. 28, 1946. Millard P. Thomas, Clerk.
By E. R., Deputy.

[Title of Superior Court and Cause.]

MOTION TO QUASH SUMMONS

The defendant above named (not appearing generally but appearing specially and solely for the purpose of this motion) moves for order quashing purported summons as issued and served by and for the plaintiff above named, upon the ground that said summons, not complying with the requirements of R.R.S. sec. 818 either in form or in substance, is insufficient and invalid to subject said defendant to the jurisdiction of the above entitled court in the above entitled action.

This motion is based upon the attached supporting affidavit, which by this reference is made a part hereof.

MERRITT, SUMMERS &
BUCEY,
LANE SUMMERS,

Attorneys for defendant above named, specially
appearing.

State of Washington,
County of King—ss.

Lane Summers, being first duly sworn, upon oath
deposes and says:

That he is a member of the firm of Merritt, Summers & Bucey and as such one of the attorneys for the Western Union Telegraph Company, a corporation, defendant above named, which is appearing not generally but specially for the purpose of the foregoing motion only.

That he has been furnished with the copy of summons in the above entitled action as prepared and issued by and for the plaintiff above named and as served upon the defendant above named, a true, full and complete copy of which same is incorporated as Exhibit A. That he has been reliably advised, and hence believes, that there has been served upon said defendant in the above entitled action no other summons or copy thereof.

That the only summons issued by said plaintiff and served upon said defendant fails to comply with R.R.S. sec. 818, prescribing the requirements of summons in unlawful detainer actions.

LANE SUMMERS.

Subscribed and sworn to before me this 14th day of November, 1946.

[Seal] W. H. HAYDEN,

Notary Public in and for the State of Washington,
residing at Seattle.

Copy received Nov. 16, 1946.

PETERSON & DUNCAN,

Attorneys for Plaintiff. (R.V.P.)

[Endorsed]: Filed Nov. 16, 1946.

[Endorsed]: Filed in United States District Court, Western District of Washington, Southern Division, Dec. 28, 1946. Millard P. Thomas, Clerk. By E. R., Deputy.

In the Superior Court of the State of Washington
in and for the County of Pierce

No. 99059

HANSEN & ROWLAND CORPORATION,
a corporation,

Plaintiff,

vs.

THE WESTERN UNION TELEGRAPH COM-
PANY, a corporation,

Defendant.

ALIAS SUMMONS

The State of Washington to The Western Union
Telegraph Company, Defendant:

You Are Hereby Summoned to appear on the
30th day of November, 1946, and defend the above
entitled action in the court aforesaid, and in case
of your failure so to do, judgment will be rendered
against you according to the demand of the com-
plaint, the original of which has been filed with the
Clerk of said court, a copy of which is herewith
attached and served upon you.

You Are Further Notified that this is an action
of unlawful detainer, and that the relief sought in
this action is to recover possession of the premises
hereinafter described for judgment for twice the
amount of rent due and of the damages that have
been and will be occasioned to the plaintiff by and

during your unlawful detention of the said premises. That the said premises in question are described as follows:

Lot Four (4), Block One Thousand Three (1003) Map of New Tacoma, W. T., Pierce County, Washington, commonly known as House No. 1007 Pacific Avenue in the City of Tacoma, Washington.

PETERSON & DUNCAN,
Attorneys for Plaintiff.

[Endorsed]: Filed Nov. 23, 1946.

[Endorsed]: Filed in the United States District Court, Western District of Washington, Southern Division, Dec. 28, 1946. Millard P. Thomas, Clerk
By E. R., Deputy.

[Title of Superior Court and Cause.]

PETITION FOR REMOVAL

To the Above Entitled Court and the Honorable
Judges Thereof:

The petition of The Western Union Telegraph Company, a corporation, sole defendant above named, respectfully shows:

I.

That the above entitled action, being a suit of a civil nature at law, of which the District Court of the United States for the Western District of

Washington, Southern Division, is given original jurisdiction, has been instituted and is now pending without trial and wholly undetermined in the above entitled court; that the action was commenced by Hansen & Rowland Corporation, a corporation, plaintiff above named, by service of alias summons (copy of which is incorporated as Exhibit A) and complaint upon the 23rd day of November, 1946, and not upon any prior date; and that the time at and before which said defendant is required by the laws of the State of Washington (specially applicable) or by the rules of the above entitled court to plead or answer to said complaint of said plaintiff has not expired, and that by such rules and such laws said defendant is allowed so to plead or answer at any time up to and including the 30th day of November, 1946.

II.

That the above entitled action, as disclosed by said complaint, makes claim and demand for double the amount of alleged rent and alleged damages, which aggregate upon the date hereof more than \$3000.00, exclusive of all interest and costs; that said defendant denies liability to said plaintiff upon its claim and demand as alleged in said complaint; and that the matter in controversy, exclusive of all interest and costs, exceeds the sum of \$3000.00.

III.

That said plaintiff always has been, and now is, a corporation organized and existing under and by virtue of the laws of the State of Washington, and

hence always has been, and now is, a citizen and resident of the State of Washington and of no other state whatsoever. That said defendant always has been, and now is, a corporation organized and existing under and by virtue of the laws of the State of New York, and hence always has been, and now is, a citizen and resident of the State of New York and of no other state whatsoever.

IV.

That said defendant is filing herewith its bond heretofore executed by it, with good and sufficient surety thereon, conditioned for said defendant entering in said District Court of the United States for the Western District of Washington, Southern Division, within thirty days from date of filing its petition for removal, a certified copy of the record in the above entitled action, and for its paying all costs that may be awarded by said District Court, if it shall hold that said action was wrongfully or improperly removed thereto.

V.

That written notice of this petition, of said bond for removal, and of said defendant's intention to file the same, together with a copy of said petition and of said bond, was given to and served upon said plaintiff, the adverse party in said action, prior to the filing of this petition and of said bond.

VI.

That the above entitled action is a controversy wholly between citizens and residents of different states.

VII.

That by reason of the premises, said defendant is entitled to have said matter removed from the above entitled Superior Court of the State of Washington, in and for the County of Pierce, unto the District Court of the United States for the Western District of Washington, Southern Division, holding terms at the City of Tacoma, in said County of Pierce, State of Washington, such being the District Court of the United States in the district where the above entitled action is pending.

MERRITT, SUMMERS &
BUCEY,

LANE SUMMERS,

Attorneys for Petitioner.

State of Washington,
County of King—ss.

Lane Summers, being first duly sworn, upon oath deposes and says:

That he is an attorney at law and a member of the firm of Merritt, Summers & Bucey, and as such one of the attorneys of record for The Western Union Telegraph Company, defendant above named, which is a non-resident corporation having no officer within the State of Washington; that all the material allegations of the foregoing petition are within his knowledge; that he makes this verification in behalf of said defendant for said reasons,

with authority so to do; that he has prepared and read said petition, which is true.

LANE SUMMERS.

Subscribed and sworn to before me this 30th day of November, 1946.

[Seal] W. H. HAYDEN,
Notary Public in and for the State of Washington,
residing at Seattle.

[Endorsed]: Filed Nov. 30, 1946.

EXHIBIT "A"

In the Superior Court of the State of Washington
in and for the County of Pierce

No. 99059

HANSEN & ROWLAND CORPORATION,
a corporation,

Plaintiff,

vs.

THE WESTERN UNION TELEGRAPH COM-
PANY, a corporation,

Defendant.

ALIAS SUMMONS

The State of Washington to The Western Union
Telegraph Company, Defendant:

You Are Hereby Summoned to appear on the
30th day of November, 1946, and defend the above

entitled action in the Court aforesaid, and in case of your failure so to do, judgment will be rendered against you according to the demand of the complaint, the original of which has been filed with the Clerk of said court, a copy of which is herewith attached and served upon you.

You Are Further Notified that this is an action of unlawful detainer, and that the relief sought in this action is to recover possession of the premises hereinafter described for judgment for twice the amount of rent due and of the damages that have been and will be occasioned to the plaintiff by and during your unlawful detention of the said premises. That the said premises in question are described as follows:

Lot Four (4), Block One Thousand Three (1003) Map of New Tacoma, W. T., Pierce County, Washington, commonly known as House No. 1007 Pacific Avenue in the City of Tacoma, Washington.

PETERSON & DUNCAN,
Attorneys for Plaintiff.

Office & P.O. Address:

520 Perkins Building

Tacoma 2, Washington

[Endorsed]: Filed in the United States District Court, Western District of Washington, Southern Division, Dec. 28, 1946. Millard P. Thomas, Clerk. By E. R., Deputy.

[Title of Superior Court and Cause.]

ORDER OF REMOVAL

The above entitled action having come regularly on for hearing before the above entitled court, the undersigned Judge presiding, this day, upon petition and bond of the defendant above named for an order transferring and removing this cause to the District Court of the United States for the Western District of Washington, Southern Division; and it appearing to the court that the defendant has filed its duly verified petition for such removal in the form required by law, and that the defendant has filed therewith its bond on removal duly and properly conditioned with good and sufficient surety for an adequate amount as provided by law, and that prior to filing said petition and said bond the said defendant had given due and legal notice thereof, of its intention to file the same, and of the time and place of presenting the same for this order, to the plaintiff above named; and it appearing to the court from an examination of the record in the above entitled action and of said petition, bond and notice, that this is a proper cause for removal to said District Court, upon the ground of diversity of citizenship and residence between the plaintiff and defendant;

Now, Therefore, said petition and bond are hereby approved and accepted, and it is hereby Ordered and Adjudged that all further proceedings in the above entitled action be, and the same hereby are, stayed, that the above entitled action be, and the same hereby is, removed to the District Court

of the United States for the Western District of Washington, Southern Division, holding terms in the City of Tacoma, Pierce County, State of Washington, and the Clerk of this Court is hereby directed to prepare and certify a true and complete transcript of the record in the above entitled action for transmission forthwith to said District Court.

Done in open court this 3rd day of December, 1946.

F. G. REMANN,
Judge.

Presented by:

CHARLES B. HOWARD,
Of Attorneys for Defendant.

Copy received Nov. 30, 1946.

PETERSON & DUNCAN,
Attorneys for Plaintiff.

[Endorsed]: Filed Dec. 3, 1946. Ent. Jour. 288,
page 363.

[Endorsed]: Filed in the United States District Court, Western District of Washington, Southern Division, Dec. 28, 1946. Millard P. Thomas, Clerk. By E. R., Deputy.

[Title of Superior Court and Cause.]

BOND ON REMOVAL

Know All Persons by These Presents:

That we, The Western Union Telegraph Company, a New York corporation, defendant above

named, as Principal, and American Surety Company of New York, as Surety, being a corporation authorized to transact business within the State of Washington, are held and firmly bound unto Hansen & Rowland Corporation, a corporation, plaintiff above named, in the sum of Five Hundred Dollars (\$500.00) lawful money of the United States, for the payment of which well and truly to be made, we, and each of us, bind ourselves, our successors and assigns, jointly and severally by these presents.

Whereas, The Western Union Telegraph Company, a New York corporation, defendant above named, is applying by petition to the Superior Court of the State of Washington for the County of Pierce for the removal of a certain action therein pending, wherein Hansen & Rowland Corporation, above named, is plaintiff, and The Western Union Telegraph Company, a New York corporation, above named, is defendant, to the District Court of the United States for the Western District of Washington, Southern Division, for further proceedings, upon the grounds set forth in said petition, and for stay of all further proceedings in said action in said Superior Court.

Now, Therefore, if The Western Union Telegraph Company, a New York corporation, shall enter in said District Court of the United States for the Western District of Washington, Southern Division, within thirty days from the date of filing said petition, a certified copy of the record in said action, and shall pay, or cause to be paid, all costs

that may be awarded therein by said District Court of the United States for the Western District of Washington, Southern Division, if said court shall hold said action was wrongfully or improperly removed thereto, then this obligation shall be void; otherwise it shall remain in full force.

Dated this 30th day of November, 1946.

Principal:

THE WESTERN UNION
TELEGRAPH COMPANY,
a New York corporation.

By MERRITT, SUMMERS &
BUCEY,
Its Attorneys.

Surety:

AMERICAN SURETY
COMPANY OF NEW YORK.

[Seal] By K. F. WARRACK,
As Its Resident
Vice-President

Attest:

B. L. LEASURE,
Resident Assistant Secretary.

[Endorsed]: Filed Nov. 30, 1946. Ent. Bond U,
page 290.

[Endorsed]: Filed in the United States District
Court, Western District of Washington, Southern
Division, Dec. 28, 1946. Millard P. Thomas, Clerk.
By E. R., Deputy.

[Title of Superior Court and Cause.]

NOTICE OF FILING PETITION AND BOND
FOR REMOVAL; PROOF OF SERVICE

To Hansen & Rowland Corporation, Plaintiff above-named, and to Peterson & Duncan, Its Attorneys:

You, and each of you, will please take notice that the Western Union Telegraph Company, a New York corporation, defendant above-named, is about to file with the Clerk of the above-entitled Court its petition and bond for removal of the above-entitled action from said Court to the District Court of the United States for the Western District of Washington, Southern Division, copy of which said petition and said bond for removal is herewith served upon you and by this reference made a part hereof; and that said defendant will present said petition and bond for removal, together with the record in the above-entitled action, if any, to the above-entitled Court, sitting within the County Court House, City of Tacoma, County of Pierce, State of Washington, upon the 5th day of December, 1946, at the hour of 10 a.m., or as soon thereafter as hearing may be had, at which time and place said defendant, through the undersigned, its attorneys, will apply for order staying further proceedings in the above-entitled Court and granting such removal of said action, and directing certified transcript of the record herein to be prepared as provided by law.

Dated at Seattle, Washington, this 30th day of November, 1946.

MERRITT, SUMMERS &
BUCEY,

LANE SUMMERS,

Attorneys for The Western Union Telegraph
Company, Defendant above named.

Service on this 30th day of November, 1946, of copy of the foregoing Notice, together with copy of said petition and of said bond for removal therein mentioned, prior to the filing of the originals thereof, is hereby acknowledged.

PETERSON & DUNCAN,
Attorneys for Plaintiff.

[Endorsed]: Filed Nov. 30, 1946.

[Endorsed]: Filed in the United States District Court, Western District of Washington, Southern Division, Dec. 28, 1946. Millard P. Thomas, Clerk. By E.R., Deputy Clerk.

In the United States District Court for the Western
District of Washington, Southern Division

No 987

HANSEN & ROWLAND CORPORATION, a
Corporation,

Plaintiff,

vs.

THE WESTERN UNION TELEGRAPH COM-
PANY, a Corporation,

Defendant.

NOTICE OF REMOVAL

To Hansen & Rowland Corporation, Plaintiff above-
named, and to Peterson & Duncan, Its Attor-
neys:

You and each of you will please take notice that on the 3rd day of December, 1946, the above-entitled action was duly removed and transferred from the Superior Court of the State of Washington, for the County of Pierce, to the District Court of the United States for the Western District of Washington, Southern Division, and that transcript of record in said action was upon the 28th day of December, 1946, duly filed in said District Court of the United

States for the Western District of Washington,
Southern Division.

Dated this 28th day of December, 1946.

MERRITT, SUMMERS &
BUCEY,

LANE SUMMERS,

Attorneys for Defendant.

Copy rec'd 12/28/46.

PETERSON & DUNCAN,
Attorneys for Plaintiff.

[Endorsed]: Filed Dec. 28, 1946.

In the Superior Court of the State of Washington
For Pierce County

No. 99059

HANSEN & ROWLAND CORPORATION, a
Corporation,

Plaintiff,

vs.

THE WESTERN UNION TELEGRAPH COM-
PANY, a Corporation,

Defendant.

CERTIFICATE ON REMOVAL TO
U. S. DISTRICT COURT

State of Washington,
County of Pierce—ss.

I, Josephine R. Melton, County Clerk, and by virtue of the laws of the State of Washington, ex-officio Clerk of the Superior Court of the State of Washington, in and for Pierce County, do hereby certify that I have compared and prepared the foregoing copy of the Summons, Complaint, Motion for Order Fixing Return day on Summons, Order, Motion to Quash Summons, Note for Motion, Brief of Defendant Specially Appearing in Support of Motion to Quash, Note of Issue, Order, Alias Summons, Motion for Order Authorizing Issuance of Alias Summons and Fixing Return Date, Order, Notice of Filing Petition and Bond for Removal;

Proof of Service, Petition for Removal, Alias Summons, Bond on Removal, Order of Removal, Stipulation and Praeceptum, to the United States District Court, for the Western District of Washington, Southern Division, at Tacoma, with the originals in the above-entitled action, now on file and of record in this office, and that the same is true and correct copy of the whole and every part of the original record in said action. Also attached are true copies of Exhibits "A," "B," "C," "D," "E" and "F" in the above-entitled cause.

In Witness Whereof, I have hereunto set my hand and affixed the seal of said Superior Court, at my office in the City of Tacoma, this 11th day of December, 1946.

[Seal] JOSEPHINE R. MELTON,
County Clerk.

By /s/ A. D. ELDER,
Deputy.

[Endorsed]: Filed in the United States District Court, Western District of Washington, Southern Division, Dec. 28, 1946. Millard P. Thomas, Clerk. By E.R., Deputy.

In the District Court of the United States for the
Western District of Washington, Southern Division

No. 987

HANSEN & ROWLAND CORPORATION, a
Corporation,

Plaintiff,

vs.

THE WESTERN UNION TELEGRAPH COM-
PANY, a Corporation,

Defendant.

MOTION TO REMAND

Now comes plaintiff and moves this court to remand the above-entitled cause to the Superior Court in and for the County of Pierce in the State of Washington on the ground that this court is without jurisdiction to hear and determine the cause, for the reason that as appears from the original complaint herein, the amount in controversy at the time of the commencement of the original action was less than Three Thousand (\$3,000.00) Dollars, exclusive of interest and costs.

This motion is based on the records and files herein.

CHARLES T. PETERSON,
WENDELL W. DUNCAN,
Attorneys for Plaintiff.

[Endorsed]: Filed Jan. 2, 1947.

[Title of District Court and Cause.]

ORDER DENYING PLAINTIFF'S MOTION
TO REMAND AND DEFENDANT'S MO-
TION TO STAY

The above-entitled action having come for hearing before the above-entitled court on the 3rd day of February, 1947, on plaintiff's motion to remand and defendant's motion to stay, and the court having become fully advised;

Now, Therefore, in conformity with oral rulings on said day, it is hereby Ordered that plaintiff's motion to remand be, and the same hereby is, denied, and that defendant's motion to stay be, and the same hereby is, denied, as to which rulings the exceptions of plaintiff and defendant, respectively, are hereby allowed.

Done in open court this 11th day of February, 1947.

CHARLES H. LEAVY,
U. S. District Judge.

Approved as to form:

By WENDELL W. DUNCAN,
Of Attorneys for Plaintiff.

Presented by:

By LANE SUMMERS,
Of Attorneys for Defendant.

[Endorsed]: Filed Feb. 11, 1947.

[Title of District Court and Cause.]

ANSWER

For answer to plaintiff's complaint, the defendant admits, denies and alleges as follows:

I.

The defendant denies each and every allegation contained in paragraph V of said complaint, except as herein expressly admitted.

The defendant admits that it received from the plaintiff notice dated July 24, 1946, a copy of which is attached and made part hereof as Exhibit 1.

II.

The defendant denies each and every allegation contained in paragraph VI of said complaint, except as herein expressly admitted.

The defendant admits that it received from the plaintiff notice dated September 25, 1946, a copy of which is attached and made part hereof as Exhibit 2.

III.

The defendant denies each and every allegation contained in paragraph VII of said complaint, except as herein expressly admitted.

The defendant admits that on October 8, 1946, it orally notified the plaintiff it was unable to vacate the premises on October 31, 1946, whereupon the plaintiff orally advised the defendant that the sum of \$750 per month was a reasonable rental value for said premises; further the defendant admits that

it received letter, a copy of which is attached and made a part hereof as Exhibit 3.

IV.

The defendant denies each and every allegation contained in paragraph VIII of said complaint, except as herein expressly admitted.

The defendant admits that on October 30, 1946, it tendered to the plaintiff as rental of said premises for the month of November, 1946, the sum of \$750, accompanying such tender by letter, a copy of which is attached and made a part hereof as Exhibit 4; further the defendant admits that on said date it notified the plaintiff it was unable to vacate said premises.

V.

The defendant denies each and every allegation contained in paragraph IX of said complaint, except as herein expressly admitted.

The defendant admits that it received notice dated November 2, 1946, a copy of which is attached and made a part hereof as Exhibit 5; further the defendant admits that it has been unable to vacate said premises.

VI.

The defendant denies each and every allegation contained in paragraph X of said complaint, except as herein expressly admitted.

The defendant admits that the principal office of the plaintiff is at Tacoma, Washington.

VII.

The defendant denies each and every allegation in

paragraph XI of said complaint, and particularly denies the plaintiff has been damaged in any sum whatsoever, as alleged or otherwise.

VIII.

The defendant alleges that on and after November 1, 1946, the sum of \$500 per month was and is the reasonable rental value of said premises, and that the sum of \$750 per month was and is excessive of the reasonable rental value of said premises; but that, nevertheless, the defendant on or before the first day of each and every month since the month of October, 1946, has made legal tenders to the plaintiff as and for rental at the rate of \$750 per months, as follows: On October 30, 1946, the sum of \$750 for the month of November, 1946; on November 30, 1946, the sum of \$1500 for the months of November and December, 1946; on December 28, 1946, the sum of \$2250, for the months of November and December, 1946, and the month of January, 1947; and on January 31, 1947, the sum of \$3000 for the months of November and December, 1946, and January and February, 1947—all of which tenders the defendant continues and renews by deposit herewith of said sum of \$3000 in the registry of the above-entitled court for the plaintiff.

IX.

The defendant alleges that for several years last prior to November 1, 1946, the agreed rental for said premises was the sum of \$325 per month, none of which was unpaid or delinquent upon or after said date; that at no time material—neither before

not after the commencement of this action—was rent, either in an agreed amount thereof or the reasonable rental value of said premises, unpaid or delinquent when due; and that the defendant is not indebted to the plaintiff in any amount on any account.

X.

The defendant alleges that at all times material it has been and is engaged in the public service of maintaining in the United States and in foreign countries, by direct ownership and operation and through indirect controls and connections, a world-wide system of communications by telegraph, cable, telephone and radio, of which its facilities installed and used upon the plaintiff's said premises continue to be an integral part and an essential link; that disruption of such service would work incalculable, irreparable damage to the public; that it has been and is burdened with mandatory duty to maintain such service and to avoid such disruption with resulting damage; that for reasons and conditions wholly beyond the defendant's power it has been unable since July 24, 1946, without breach of such duty, to remove its equipment and to vacate said premises, despite definite wish and diligent preparation so to do; and that of such facts the plaintiff has been and is fully aware.

XI.

The defendant alleges that upon its vacation of said premises and before any subsequent occupancy thereof the plaintiff has been and is intending and

planning to remodel the same, for which purpose it applied to the Civilian Production Administration of the United States for permit, which was granted only upon condition (imposed for the protection of the defendant's said service to the public) that the work of remodeling be not commenced before December 1, 1946, to which condition the plaintiff agreed.

XII.

The defendant alleges that the prior unlawfulness, if any, of its possession of said premises was waived by the plaintiff's demand on November 2, 1946, for rent declared by it to have become due and payable on November 1, 1946.

Wherefore, the defendant prays that plaintiff's action be dismissed, and that defendant have such other relief as may be just and proper, together with its costs and disbursements.

MERRITT, SUMMERS &
BUCEY.

LANE SUMMERS,

Attorneys for Defendant.

Copy received Feb. 11, 1947.

PETERSON & DUNCAN,
Attorneys for Plaintiff.

[Endorsed]: Filed Feb. 11, 1947.

[Title of District Court and Cause.]

STIPULATION OF FACTS

By and between plaintiff and defendant, in lieu of evidence and as the factual basis for judgment of the above-entitled court in the above-entitled action, it is hereby agreed:

1. That at all times material the plaintiff, a Washington corporation, was the owner of certain premises commonly known as 1007 Pacific Avenue in the City of Tacoma (being Lot 4, Block 1003, of the Map of New Tacoma, W.T.); and at all times material to and including the 31st day of October, 1946, the defendant, a New York corporation, engaged in the service of operating a world-wide system of communications, was the lessee of said premises in lawful possession thereof under valid lease as extended. That said premises were not leased or used for living or residential purposes.

2. That the defendant received from the plaintiff notice dated July 24, 1946, a copy of which is hereunto attached as Exhibit 1.

3. That the defendant received from the plaintiff notice dated September 25, 1946, a copy of which is hereunto attached as Exhibit 2.

4. That on October 8, 1946, the defendant orally notified the plaintiff that it was unable to vacate the premises on October 31, 1946, whereupon the plaintiff orally advised the defendant that the sum of \$750 per month was a reasonable rental value of

said premises. That thereafter the defendant received letter, a copy of which is hereunto attached as Exhibit 3.

5. That on October 30, 1946, the defendant tendered to the plaintiff as rental of said premises for the month of November, 1946, the sum of \$750.00, accompanying such tender by letter, a copy of which is hereunto attached as Exhibit 4. That on October 30, 1946, the defendant notified the plaintiff it was unable to vacate said premises.

6. That the defendant received notice dated November 2, 1946, a copy of which is hereunto attached as Exhibit 5. That the defendant was unable to vacate said premises.

7. That the plaintiff is not engaged in the insurance business in the City of Tacoma or the State of Washington and is not authorized or licensed so to do. That the plaintiff suffered no special damages as alleged by its complaint or otherwise, and is not entitled to recovery thereof.

8. That no rent under lease as extended was due or owing from the defendant to the plaintiff on October 31, 1946, all rent under said lease as extended having been previously paid in full.

9. That on the 30th day of November, 1946, the defendant tendered to the plaintiff the sum of \$1500.00 as rental for the months of November and December, 1946, and accompanied such tender by letter, a copy of which is hereunto attached as Exhibit 6.

That on the 28th day of December, 1946, the defendant tendered to the plaintiff the sum of \$2250.00 as rental for the months of November and December, 1946, and January, 1947, and accompanied such tender by letter, a copy of which is hereunto attached as Exhibit 7.

That on the 31st day of January, 1947, the defendant tendered to the plaintiff the sum of \$3000.00 as rental for the months of November and December, 1946, and January and February, 1947, and accompanied such tender by letter, a copy of which is hereunto attached as Exhibit 8.

That on the 11th day of February, 1947, the defendant filed its answer to the plaintiff's complaint in the above-entitled cause, and contemporaneously therewith deposited in the registry of the above-entitled court, in perpetuation of tenders previously made, the sum of \$3000.00.

That on the 28th day of February, 1947, the defendant tendered to the plaintiff the sum of \$750 as rental for the month of March, 1947, accompanied by letter, a copy of which is hereunto attached as Exhibit 9; that thereafter on said date the defendant deposited said sum of \$750 in the registry of the above-entitled court in perpetuation of such tender.

10. That at all times material on and after the first day of November, 1946, the reasonable rental value of said premises was the sum of \$750 per month.

11. That on the 7th day of March, 1947, said premises were completely vacated by the defendant and possession thereof entirely surrendered to the plaintiff.

Dated this 6th day of May, 1947.

CHARLES T. PETERSON,
WENDELL W. DUNCAN,
Attorneys for Plaintiff.

MERRITT, SUMMERS &
BUCEY,
LANE SUMMERS.
Attorneys for Defendant.

EXHIBIT 1

[Letterhead Hansen & Rowland, Inc.]

Tacoma, Washington, July 24, 1946

The Western Union Telegraph Company, Executive
Offices, 60 Hudson Street, New York, N. Y.

Gentlemen:

Reference is hereby made to that certain written lease dated December 2, 1932, between Premier Investment Company, party of the first part, and The Western Union Telegraph Company, party of the second part, and pertaining to certain premises at 1007 Pacific Avenue in the City of Tacoma, Washington, as in said lease more fully described, and which said lease was for the term commencing November 1, 1932, and terminating on October 31, 1938, and which said was thereafter by a written

agreement between Western Union Realty Corporation (successor in interest to Premier Investment Company) and The Western Union Telegraph Company renewed and extended for a further period of three years from the first day of November, 1938, to October 31, 1941, and again thereafter by written instrument dated February 27, 1941, between the said parties renewed and extended for an additional period of five years from the first day of November, 1941, and ending October 31, 1946.

The undersigned, Hansen & Rowland Corporation, present owner of said leased premises and the successor in interest to said Western Union Realty Corporation in said above described lease, being desirous of terminating said lease at the end of its said term as above described, does now hereby pursuant to the provisions of said lease notify you of its desire and intent to so terminate said lease at the end of its said term, to-wit, October 31, 1946.

A signed duplicate of this notice is being forwarded to the office of the District Superintendent at Portland, Oregon.

Very truly yours,

HANSEN & ROWLAND
CORPORATION,

By H. T. HANSEN,
President.

HTH:ft

CC The Western Union Telegraph Company Attention: Mr. R. H. Cobb, District Superintendent, 239 Southwest Broadway, Portland Oregon.

EXHIBIT 2

NOTICE

To:

Western Union Telegraph Company
Tenants in possession of premises at
1007 Pacific Avenue
Tacoma, Washington

Please Take Notice that the undersigned owner of the following described real property in Pierce County, Washington, to-wit:

Lot Four (4) in Block One Thousand Three (1003) Map of New Tacoma, W.T., in Pierce County, Washington,

commonly known as House No. 1007 Pacific Avenue in the City of Tacoma, Washington, hereby notifies you that you are hereby required to quit and surrender up to the undersigned owner entitled thereto the possession of the above-entitled premises now occupied by you as tenant, at the expiration of your tenancy on the first day of November, 1946.

Dated at Tacoma, Washington, September 25th, 1946.

HANSEN & ROWLAND
CORPORATION,

By CHARLES T. PETERSON,
Agent and Attorney.

EXHIBIT 3

Tacoma, Washington

October 8, 1946

Western Union Telegraph Company

1007 Pacific Avenue

Tacoma, Washington

Attention: Mr. R. H. Cobb.

Gentlemen:

Referring to your continuing in possession of the premises at 1007 Pacific Avenue, Tacoma, Washington, after October 31st, 1946, please be advised that you may continue such possession for a period not exceeding four months after the expiration of the present lease on the following terms and conditions.

You are to pay, in advance, rental at the rate of \$1500 per month, monthly; however, you shall have the option and privilege of vacating and surrendering up the premises at any time during the month, providing you give the owners ten days' written notice of your intention and desire so to do, and upon vacating, the unearned portion of any month's rental will be refunded to you.

Conditions of space in the City of Tacoma are such that it was necessary for the owners to move one of the departments of their business to Seattle pending the time they can get possession of said premises. They regard the premises as having a reasonable rental value of \$750.00 per month and

the moving of this department to Seattle so that it may be kept intact, and employing of additional help incident to having one branch of their business done in Seattle, will cost at least \$750.00 per month, and undoubtedly, considering the cost of moving, more than that amount.

If you desire to avail yourself of this proposal, you may do so by endorsing your acceptance hereon and returning same to writer.

HANSEN & ROWLAND, INC.,

By CHARLES T. PETERSON,

Agent and Attorney.

We hereby accept and agree to the foregoing:

WESTERN UNION TELE-
GRAPH COMPANY,

By

EXHIBIT 4

Oct. 30, 1946

Hansen & Rowland Corporation

Hansen & Rowland, Inc.

Tacoma, Washington

Gentlemen:

Re: 1007 Pacific Avenue—Western Union
Telegraph Company office space

Herewith is tendered the sum of Seven Hundred and Fifty Dollars in U. S. currency, covering rental

for the month of November, 1946—that amount having been claimed and demanded by your letter of October 8, 1946, as the reasonable monthly rental value of the space above mentioned, which this company is compelled by circumstances to occupy until vacation is possible.

Yours very truly,

WESTERN UNION TELE-
GRAPH COMPANY,

By MERRITT, SUMMERS &
BUCEY,

LS/ley

Its Attorneys.

EXHIBIT 5

NOTICE

To: Western Union Telegraph Company, Tenants
in possession of premises at 1007 Pacific Avenue
Tacoma, Washington

Please take notice that you are hereby required to pay the rental of \$1500.00, which became due and payable on the 1st day of November, 1946, as rental for the premises now occupied by you, to-wit:

Lot Four (4) in Block One Thousand Three
(1003) Map of New Tacoma, W.T., in Pierce
County, Washington,

commonly known as house No. 1007 Pacific Avenue
in the City of Tacoma, Washington, within three
days following the date of service of this notice, or

in the alternative, to quit, vacate and surrender up to the undersigned owners thereof possession of said premises.

Please govern yourself accordingly.

Dated at Tacoma, Washington, November 2, 1946.

HANSEN & ROWLAND
CORPORATION,
By CHARLES T. PETERSON,
Its Agent and Attorney.

EXHIBIT 6

Nov. 30, 1946

Hansen & Rowland Corporation, C/o Peterson &
Duncan, Attorneys, 520 Perkins Building,
Tacoma, Washington

Gentlemen:

Re: 1007 Pacific Avenue—office space

Herewith is tendered the sum of \$1500 in United States currency covering office space rental for the months of November and December, 1946, at the rate of \$750 per month, claimed by you as the reasonable rental value thereof according to your letter of October 8, 1946.

Very truly yours,

THE WESTERN UNION
TELEGRAPH COMPANY,
By MERRITT, SUMMERS &
BUCEY,

LS/KT

As Its Attorneys.

EXHIBIT 7

Dec. 28, 1946

Hansen & Rowland Corporation
C/o Peterson & Duncan, Attorneys,
520 Perkins Building
Tacoma, Washington

Gentlemen:

Re: 1007 Pacific Avenue—office space

Herewith is tendered the sum of \$2250.00 in United States currency covering office space rental for the months of November and December, 1946, and January, 1947, at the rate of \$750 per month, claimed by you as the reasonable rental value thereof according to your letter of October 8, 1946.

Very truly yours,

THE WESTERN UNION
TELEGRAPH COMPANY,

By MERRITT, SUMMERS &
BUCEY,

As Its Attorneys.

LS/KT

EXHIBIT 8

Jan. 30 1947

Hansen & Rowland Corporation,
C/o Peterson & Duncan, Attorneys
520 Perkins Building,
Tacoma, Washington

Gentlemen :

Re: 1007 Pacific Avenue—office space

Herewith is tendered the sum of \$3000.00 in United States currency covering office space rental for the months of November and December, 1946, and January and February, 1947, at the rate of \$750 per month, claimed by you as the reasonable rental value thereof according to your letter of October 8, 1946.

Very truly yours,

THE WESTERN UNION
TELEGRAPH COMPANY,

By MERRITT, SUMMERS &
BUCEY,

As Its Attorneys.

LS/KT

EXHIBIT 9

Feb. 28, 1947

Hansen & Rowland Corporation,
C/o Peterson & Duncan, Attorneys
520 Perkins Bldg.
Tacoma, Washington

Gentlemen:

Re: 1007 Pacific Avenue—office space

Herewith is tendered the sum of \$750.00 in United States currency covering office space rental for the month of March, 1947, at the rate of \$750 per month, claimed by you as the reasonable rental value thereof according to your letter of October 8, 1946.

Very truly yours,

THE WESTERN UNION
TELEGRAPH COMPANY,

By MERRITT, SUMMERS &
BUCEY,

As Its Attorneys.

LS/KT

[Endorsed]: Filed May 6, 1947.

[Title of District Court and Cause.]

DEFENDANT'S DISAPPROVAL OF AND OBJECTIONS TO PROPOSED FINDINGS OF FACT.

The defendant disapproves of findings as proposed by the plaintiff because they are not completely in harmony with the undenied allegations of the pleadings and the stipulation of facts; and in addition defendant specifically objects to such proposed findings of fact as follows:

1. Because no proposed finding is based upon paragraph 3 of the stipulation of facts and upon Exhibit 2 attached thereto.

2. Because proposed finding number 4 does not adhere to paragraph 4 of the stipulation of facts, and does not incorporate all of the plaintiff's letter of October 8, 1946, attached thereto as Exhibit 3.

3. Because proposed finding number 6 does not adhere to paragraph 5 of the stipulation of facts, does not incorporate all of the defendant's letter of October 30, 1946, attached thereto as Exhibit 4, and does not find that the plaintiff was then notified by the defendant it was unable to vacate said premises.

4. Because proposed finding number 7 does not adhere to paragraph 6 of the stipulation of facts, does not incorporate all of plaintiff's notice of November 2, 1946, attached thereto as Exhibit 5, and

does not find that the defendant was unable to vacate said premises; and because proposed finding number 7 contains recital in the nature of a conclusion of law.

5. Because proposed finding number 8 is contrary to facts as stipulated to the extent of \$750.

6. Because proposed finding number 9 is contrary to the ruling of this court as to the date of the commencement of plaintiff's action, and is contrary to the allegations and prayer of the plaintiff's complaint; and because proposed finding number 9 is unnecessary, since the record speaks for itself.

7. Because proposed finding number 10 does not adhere to paragraph 9 of the stipulation of facts, and does not incorporate the defendant's letters of tender attached thereto as Exhibits 6, 7, 8 and 9.

8. Because no proposed finding is based upon paragraph 7 of the stipulation of facts.

9. Because no proposed finding is based upon paragraph 8 of the stipulation of facts.

MERRITT, SUMMERS &

BUCEY,

LANE SUMMERS,

Attorneys for Defendant.

[Endorsed]: Filed May 27, 1947.

[Title of District Court and Cause.]

DEFENDANT'S DISAPPROVAL OF AND OB-
JECTIONS TO PROPOSED CONCLU-
SIONS OF LAW.

Defendant disapproves of conclusions of law as proposed by the plaintiff and objects specifically thereto as follows:

1. Because proposed conclusion number 1 is contrary to and unsupported by the stipulation of facts and is unwarranted in law.

2. Because proposed conclusion number 3 is contrary to and unsupported by the stipulation of facts and is unwarranted in law.

MERRITT, SUMMERS &
BUCEY,
LANE SUMMERS,
Attorneys for Defendant.

[Endorsed]: Filed May 27, 1947.

[Title of District Court and Cause.]

DEFENDANT'S DISAPPROVAL OF AND
OBJECTIONS TO PROPOSED JUDGMENT

The defendant disapproves of judgment as proposed by the plaintiff and objects thereto because said proposed judgment is contrary to and unsupported by the undenied allegations of the pleadings,

the stipulation of facts, and the law applicable thereto.

MERRITT, SUMMERS &
BUCEY,
LANE SUMMERS,
Attorneys for Defendant.

[Endorsed]: Filed May 27, 1947.

[Title of District Court and Cause.]

FINDINGS OF FACT AS PROPOSED BY
DEFENDANT (REFUSED)

This action having regularly come to trial on the 19th day of May, 1947, before the above entitled court, the undersigned judge presiding, without a jury, and the plaintiff appearing by Charles T. Peterson of Peterson & Duncan, its attorneys, the defendant appearing by Lane Summers of Merritt, Summers & Bucey, its attorneys, stipulation of facts in lieu of evidence as factual basis for judgment having been signed by the plaintiff and the defendant, having been filed, and having been considered by the court, argument having been heard, and the court having become fully advised,

Hereby makes Findings of Fact by adopting as such said stipulation of facts; and

Hereby draws Conclusions of Law as follows:

1. That the plaintiff by its notice dated November 2nd, 1946 (Exhibit 5), operating retroactively,

elected to treat the defendant not as a trespasser but as a tenant on and after November 1st, 1946, when, in the absence of agreement between the plaintiff and the defendant as to the rate of rent, the defendant occupied the premises as a tenant by sufferance.

2. That the defendant having made timely tenders to the plaintiff and deposits in court of the reasonable rental value of the premises at the rate of \$750 per month from November 1, 1946, to March 7, 1947, both inclusive, in the total sum of \$3175, has satisfied its obligation to the plaintiff.

3. That the defendant is not guilty of unlawful detainer and hence is not liable for statutory penalty.

4. That the defendant is entitled to judgment awarding from deposit in court in the total sum of \$3750, to the plaintiff the sum of \$3175, and to the defendant the sum of \$575.

Dated this day of, 1947.

U. S. District Judge.

Presented by:

Of Counsel for Defendant.

[Endorsed]: Filed June 2, 1947.

In the United States District Court for the Western
District of Washington, Southern Division

No. 987

HANSEN & ROWLAND CORPORATION,
a corporation,

Plaintiff,

vs.

THE WESTERN UNION TELEGRAPH
COMPANY,

Defendant.

JUDGMENT AS PROPOSED BY
DEFENDANT (REFUSED)

This action having regularly come to trial on the 19th day of May, 1947, before the above entitled court, the undersigned judge presiding, without a jury, the plaintiff appearing by Charles T. Peterson of Peterson & Duncan, its attorneys, the defendant appearing by Lane Summers of Merritt, Summers & Bucey, its attorneys, stipulation of facts in lieu of evidence as factual basis for judgment having been signed by the plaintiff and the defendant, having been filed, and having been considered by the court, together with argument of counsel, and the court being fully advised;

Now, Therefore, based on findings of fact and conclusions of law heretofore made and drawn this day, it is hereby Ordered, Considered and Adjudged

that from deposit in the registry of the court in the above entitled cause in the total sum of \$3750, the Clerk make payments as follows: to the plaintiff the sum of \$3175, and to the defendant the sum of \$575; and that the defendant have its costs and disbursements herein to be taxed.

Done in open court this day of,
1947.

U. S. District Judge.

Presented by:

Of counsel for Defendant.

[Endorsed]: Filed June 2, 1947.

[Title of District Court and Cause.]

FINDINGS OF FACT AND CONCLUSIONS OF LAW

This matter coming on regularly for trial on the 19th day of May, 1947, before the above entitled court, sitting without a jury, the plaintiff appearing by Charles T. Peterson of Peterson & Duncan, its attorneys, defendant appearing by Lane Summers of Merritt, Summers & Bucey, attorneys for defendant. The plaintiff and defendant having entered into a stipulation of facts in lieu of evidence as the factual basis for judgment of the court, which stipulation was duly filed herein, and the court having considered said stipulation of facts, and

after hearing argument of counsel, and being fully advised in the premises announced that it would find in favor of plaintiff and against defendant, and in accordance therewith the court doth now make the following

Findings of Fact

1. That at all times material the plaintiff, a Washington corporation, was the owner of certain premises commonly known as 1007 Pacific Avenue in the City of Tacoma (being Lot 4, Block 1003, of the Map of New Tacoma, W. T.); and at all times material to and including the 31st day of October, 1946, the defendant, a New York corporation engaged in the service of operating a world-wide system of communications, was the lessee of said premises in lawful possession thereof under valid lease as extended, which said lease was made December 2, 1932, by plaintiff's predecessor in interest for a period of five years and was renewed on an annual basis, the last of which renewals expired on the 31st day of October, 1946.

2. That said premises were not leased or used for living or residential purposes.

3. That said original lease, as extended, provided that either party thereto shall give to the other, at least three months before the end of any term, notice of its desire and intent to terminate said lease at the end of said term. That accordingly on July 24, 1946, plaintiff gave defendant written notice of its desire to terminate said lease at the end of the current term which expired on October 31, 1946.

4. That on October 8, 1946, defendant orally notified plaintiff that it was unable to vacate said premises on October 31, 1946; whereupon plaintiff notified defendant orally and in writing that it would be permitted to continue in possession of said premises for a period not exceeding four months after the expiration of said term, providing defendant paid an advance rental for said premises at the rate of \$1500.00 monthly, with the option and privilege on the part of defendant to vacate and surrender up said premises at any time during the month, providing defendant gave plaintiff ten days written notice of its intention and desire so to do, in which event the unearned portion of any month's rental would be refunded by plaintiff to defendant; and in said written proposal requested defendant if it desired to avail itself of said proposal to do so by endorsing its acceptance thereon and returning the same to plaintiff's agent and attorney.

5. The defendant did not endorse its acceptance on said proposal nor return the same so endorsed to plaintiff's attorney.

6. That on October 30, 1946, defendant tendered to plaintiff the sum of \$750.00 as the reasonable rental value of said premises, which tender was accompanied by a letter in writing, which tender plaintiff refused.

7. That on November 2, 1946, plaintiff caused a notice in writing to be served on defendant, by the terms of which notice defendant was required to pay the rental of \$1500.00, which plaintiff stated became due and payable on November 1, 1946, as rental for said premises within three days following the date of service of said notice, or in the alternative to quit, vacate and surrender up to the owner the possession of said premises.

8. That defendant failed to pay said requested rental of \$1500.00 within said three days, or at all, and continued in the possession of said premises.

9. That on November 9, 1946, plaintiff brought this action to recover the possession of said premises and to oust defendant therefrom, and for damages and penalty for the unlawful detainer of said premises.

10. That defendant timely tendered the sum of \$750.00 to plaintiff as the reasonable rental for said premises for the months of November, December, January, February and March, accompanying the tender in each instance by a written letter, which tenders plaintiff refused, whereupon defendant paid same into the registry of this court.

11. That at all times material on and after the 1st day of November, 1946, the reasonable rental value of said premises so occupied and detained by defendant was \$750.00 per month.

12. That on the 7th day of March, 1947, defendant vacated and surrendered up possession of said premises to plaintiff.

From the foregoing Findings of Fact the court makes the following

Conclusions of Law

1. That defendant wrongfully held and detained the possession of said premises and every part thereof from plaintiff at all times from and including the 1st day of November, 1946, to and including the 7th day of March, 1946.

2. That the reasonable rental value of said premises for said period was \$750.00 per month, or a total of \$3175.00.

3. That by reason of defendant's wrongful detainer of said premises during said period, plaintiff is entitled to a judgment in double the amount of the reasonable rental of said premises during said period, to wit, judgment in the amount of \$6,350.00, together with costs of suit. Let judgment be entered accordingly.

Dated this 2nd day of June, 1947.

Exceptions allowed to the defendants. (C. H. L.)

CHARLES H. LEAVY,

United States District Judge.

Presented by:

Of Counsel for Plaintiff.

[Endorsed]: Filed June 2, 1946.

In the United States District Court for the Western
District of Washington, Southern Division

No. 987

HANSEN & ROWLAND CORPORATION

a corporation,

Plaintiff,

vs.

THE WESTERN UNION TELEGRAPH COM-
PANY, a corporation,

Defendant.

JUDGMENT

This matter coming on regularly for trial on the 19th day of May, 1947, before the above entitled court, sitting without a jury, the plaintiff appearing by Charles T. Peterson of Peterson & Duncan, its attorneys, defendant appearing by Lane Summers of Merritt, Summers & Bucey, attorneys for defendant. The plaintiff and defendant having entered into a stipulation of facts in lieu of evidence as the factual basis for judgment of the court, which stipulation was duly filed herein, and the court having considered said stipulation of facts, and after hearing argument of counsel, and being fully advised in the premises announced that it would find in favor of plaintiff and against defendant, and having made its Findings of Fact and Conclusions of Law herein in writing, wherein and whereby it found, all and singular the facts, it is now, in accordance therewith,

Ordered, Adjudged and Decreed that plaintiff, Hansen & Rowland Corporation, a Washington corporation, do have and recover of and from the Western Union Telegraph Company, a corporation, defendant herein, a New York corporation, the sum of \$6,350.00, with interest thereon from date hereof, together with costs of suit to be taxed. Exceptions allowed defendants. (C. H. L.)

Dated June 2nd, 1947.

CHARLES. H. LEAVY,
United States District Judge.

Presented by:

Of Counsel for Plaintiff.

[Endorsed]: Filed June 2, 1947.

[Title of District Court and Cause.]

DEFENDANT'S EXCEPTIONS TO FINDINGS, CONCLUSIONS AND JUDGMENT

Findings of fact, conclusions of law and judgment, as proposed by the plaintiff, having been signed and entered by the above entitled court on the 2nd day of June, 1947, in the absence of attorneys for either the plaintiff or the defendant, now the defendant excepts to said findings, conclusions and judgment in the above entitled cause for the reasons heretofore assigned by defendant's disapproval of and objections to the same, and for the reason that said findings, conclusions and judgment are contrary to the undisputed facts and the applicable law in the above entitled action.

Dated this 3rd day of June, 1947.

MERRITT, SUMMERS &
BUCEY,
LANE SUMMERS,
Attorneys for Defendant.

Copy received June 4, 1947.

PETERSON & DUNCAN,
Attorneys for Plaintiff.

[Endorsed]: Filed June 4, 1947.

[Title of District Court and Cause.]

STIPULATION

Whereas, judgment was entered by the above entitled court in the above entitled action on the 2nd day of June, 1947, in favor of the plaintiff and against the defendant in the amount of \$6350.00, together with costs;

Whereas, defendant intends to appeal from said judgment to the United States Circuit Court of Appeals for the Ninth Circuit;

Whereas, the defendant concedes it is indebted to the plaintiff in the sum of \$3175.00 but not in any greater amount, which sum has been paid by it into the registry of the court; and

Whereas, it is the desire of both the plaintiff and the defendant to minimize the amount of supersedeas bond;

Now, Therefore, the plaintiff and the defendant agree:

1. That the sum of \$3175.00 heretofore paid by the defendant into the registry of the court may, without prejudice to the rights of either party on said appeal, be forthwith paid to the plaintiff.

2. That on said appeal supersedeas bond in the sum of \$4000.00 shall be sufficient as to amount.

3. That if said judgment of the above entitled court is affirmed on said appeal, said sum of \$3175.00 so paid shall be regarded as partial satisfaction of final judgment in the above entitled cause, and shall not bear interest.

4. That if said judgment of the above entitled court is reversed or modified on said appeal, said

sum of \$3175.00 so paid shall be taken into account in adjustment thereunder of the rights of plaintiff and defendant.

5. That this stipulation and any order of the court entered in pursuance hereof shall in no wise affect or prejudice the rights of either plaintiff or defendant on said appeal, and the rights of the plaintiff and defendant with respect to said appeal shall in all particulars be preserved as fully and for all purposes as though this stipulation were never made nor any order entered by the above entitled court in pursuance thereof.

Dated this 10th day of June, 1947.

PETERSON & DUNCAN,
Attorneys for Plaintiff.

MERRITT, SUMMERS &
BUCEY,
Attorneys for Defendant.

[Endorsed]: Filed June 11, 1947.

[Title of District Court and Cause.]

ORDER ALLOWING WITHDRAWAL OF
FUNDS IN REGISTRY OF COURT

Plaintiff and defendant having filed stipulation from which it appears that defendant intends to prosecute an appeal from the judgment of the above entitled court, entered in the above entitled action on the 2nd day of June, 1947, in favor of the plaintiff and against the defendant in the amount of \$6350.00, together with costs, by which stipulation it is agreed that the sum of \$3175.00,

but no more, heretofore deposited in the registry of the court, may be withdrawn by and paid to the plaintiff in minimization of supersedeas bond to be filed by the defendant on said appeal, such withdrawal and payment to be without prejudice to the rights of either plaintiff or defendant on said appeal;

Now, Therefore, it is hereby Ordered that the Clerk of the above entitled court is authorized and directed forthwith to pay said sum of \$3175.00 to the plaintiff, Hansen and Rowland Corporation, or its attorneys, Peterson & Duncan, and that such payment shall not affect or prejudice the rights of either the plaintiff or the defendant with respect to said appeal.

Dated this 11th day of June, 1947.

CHARLES H. LEAVY,

United States District Judge.

Approved by:

LANE SUMMERS,

Of Attorneys for Defendant.

Presented by:

PETERSON & DUNCAN,

Of Attorneys for Plaintiff.

Received this 16th day of June, 1947, check of Treasurer of the United States #5,480, in the sum of \$3,175.00.

PETERSON & DUNCAN,

Attorneys for Plaintiff,

By W. W. DUNCAN.

[Endorsed]: Filed June 11, 1947.

[Title of District Court and Cause.]

NOTICE OF APPEAL

To the Clerk of the above entitled Court, to Hansen
& Rowland Corporation, Plaintiff above named;
and to Peterson & Duncan, its attorneys:

Notice is given that The Western Union Telegraph
Company, the defendant above named, hereby ap-
peals to the United States Circuit Court of Appeals
for the Ninth Circuit from that certain judgment
entered upon the 2nd day of June, 1947, in favor
of said plaintiff against said defendant in the above
entitled action by the above entitled court.

Dated this 10th day of June, 1947.

MERRITT, SUMMERS &
BUCEY,

LANE SUMMERS,
Attorneys for Defendant.

Copy received June 11, 1947.

PETERSON & DUNCAN,
Attorneys for Plaintiff.

Copy of the within and foregoing Notice of Ap-
peal mailed to Messrs. Peterson & Duncan, attor-
neys for Plaintiff, at Perkins Building, Tacoma,
Washington, this 12th day of June, 1947.

E. E. REDMAYNE,
Deputy Clerk.

[Endorsed]: Filed June 11, 1947.

[Title of District Court and Cause.]

SUPERSEDEAS BOND ON APPEAL

Know All Persons By These Presents:

That The Western Union Telegraph Company, as Principal, and Fidelity and Deposit Company of Maryland, a corporation authorized to do business within the State of Washington, as Surety, are held and firmly bound unto Hansen & Rowland Corporation, in the full sum of Four Thousand Dollars (\$4000.00) for the payment of which well and truly to be made we bind ourselves, our successors and assigns, jointly and severally by these presents.

Whereas, in the above entitled action judgment was rendered in favor of Hansen & Rowland Corporation against The Western Union Telegraph Company for the sum of \$6350.00, plus interest and costs, from which judgment The Western Union Telegraph Company is appealing to the United States Circuit Court of Appeals for the Ninth Circuit in the time and manner provided by law, pending which appeal it desires to stay and supersede said judgment until determination thereof by said appellate court;

Now, Therefore, the condition of the foregoing bond is such that if The Western Union Telegraph Company as such Principal shall prosecute its appeal to effect, shall satisfy in full said judgment (or any modification thereof by said appellate court), together with all costs, interest and damages for delay if for any reason said appeal be dismissed or

said judgment be affirmed or modified, and also shall satisfy in full all costs, interest and any damages awarded against it by said appellate court, then this bond shall be void; otherwise it shall continue in full force and effect.

Dated this 10th day of June, 1947, at Seattle, Washington.

(Principal)
THE WESTERN UNION
TELEGRAPH COMPANY,
By MERRITT, SUMMERS &
BUCEY,
Its Attorneys.

(Surety)
FIDELITY AND DEPOSIT
COMPANY OF MARYLAND.

[Seal] /s/ By S. W. HOLBROOK,
Attorney-in-Fact.

The foregoing bond is hereby approved as to form, amount and surety.

PETERSON & DUNCAN,
Attorneys for Plaintiff.

The foregoing bond is hereby approved, and stay of proceedings upon judgment of the above entitled court pending the appellate court's determination of appeal therefrom is hereby granted.

Done in open court this 12th day of June, 1947.

CHARLES H. LEAVY,
United States District Judge.

[Endorsed]: Filed June 11, 1947.

United States Circuit Court of Appeals
for the Ninth Circuit

No. 987

THE WESTERN UNION TELEGRAPH
COMPANY, a corporation,

Appellant,

vs.

HANSEN & ROWLAND CORPORATION,
a corporation,

Appellee.

STIPULATION AS TO RECORD

In substitution for appellant's designation of a portion of the record and for the elimination of all unessential material, by appellant above named and appellee above named it is hereby stipulated:

(A) That the record on appeal in the above entitled action shall include the following:

- (1) Complaint with Exhibit F only;
- (2) Original summons, returnable November 18, 1946;
- (3) Motion to quash summons;
- (4) Alias summons, returnable November 30, 1946;
- (5) Petition for removal;
- (6) Bond on removal;
- (7) Notice of filing petition and bond on removal; proof of service;
- (8) Order of removal;
- (9) Notice of removal;

- (10) Clerk's certificate on removal;
- (11) Motion to remand;
- (12) Order denying motion to remand;
- (13) Answer to complaint, with no exhibits;
- (14) Stipulation of facts, with all exhibits;
- (15) Defendant's disapproval of and objections to proposed findings of fact;
- (16) Defendant's disapproval of and objections to proposed conclusions of law;
- (17) Defendant's disapproval of and objections to proposed judgment;
- (18) Findings of fact and conclusions of law as proposed by defendant and refused by the court;
- (19) Judgment as proposed by the defendant and refused by the court;
- (20) Findings of fact and conclusions of law as signed by the court on June 2, 1947;
- (21) Judgment as signed by the court on June 2nd, 1947;
- (22) Defendant's exceptions to findings, conclusions and judgment as signed and entered on June 2nd, 1947;
- (23) Stipulation as to withdrawal of funds;
- (24) Order of court allowing withdrawal of funds;
- (25) Notice of appeal;
- (26) Bond on appeal;
- (27) This stipulation;
- (28) Appellant's statement of points;
- (29) Appropriate notation of service and filing dates.

(B) That the record on appeal in the above entitled action shall exclude the following:

(1) All portions of the record not listed above.

Dated this 30th day of June, 1947.

MERRITT, SUMMERS &
BUCEY,
LANE SUMMERS,
Attorneys for Appellant.

PETERSON & DUNCAN,
/s/ WENDELL W. DUNCAN,
Attorneys for Appellee.

To the Clerk of the United States District Court for
the Western District of Washington, Southern
Division:

You will please prepare and certify record on
appeal in the above entitled action in harmony with
the foregoing stipulation relative thereto.

Dated this 30th day of June, 1947.

MERRITT, SUMMERS &
BUCEY,
LANE SUMMERS,
Attorneys for Appellant.

[Endorsed]: Filed U. S. D. C. June 30, 1947.

[Title of Circuit Court of Appeals and Cause.]

APPELLANT'S STATEMENT OF POINTS

The Western Union Telegraph Company, appellant above named, upon its appeal in the above entitled action relies upon the following points:

(1) Error by the District Court in refusing findings of fact as proposed by the defendant;

(2) Error by the District Court in refusing conclusions of law as proposed by the defendant;

(3) Error by the District Court in refusing judgment as proposed by the defendant;

(4) Error by the District Court in disregarding defendant's disapproval of and objections to findings, conclusions and judgment as proposed by the plaintiff;

(5) Error by the District Court in making findings, drawing conclusions and allowing judgment as signed and filed by the court on June 2nd, 1947;

(6) Error by the District Court in finding and concluding that the defendant was guilty of unlawful detainer under the statutes of the State of Washington;

(7) Error by the District Court in granting judgment against the defendant for unlawful detainer penalty under the statutes of the State of Washington;

(8) Error by the District Court in failing to exonerate the defendant from all obligations to the

plaintiff in excess of the sum of \$3175.00 on deposit in the registry of the court.

Dated this 30th of June, 1947.

MERRITT, SUMMERS &
BUCEY,
LANE SUMMERS,
Attorneys for Appellant.

Copy received June 30th, 1947.

PETERSON & DUNCAN,
Attorneys for Appellee.

[Endorsed]: Filed U. S. D. C. June 30, 1947.

In the United States District Court for the Western
District of Washington, Southern Division
Civil No. 987

HANSEN & ROWLAND CORPORATION,
a corporation,

Plaintiff,

vs.

THE WESTERN UNION TELEGRAPH
COMPANY, a corporation,

Defendant.

United States of America,
Western District of Washington—ss.

CLERK'S CERTIFICATE TO RECORD
ON APPEAL

I, Millard P. Thomas, Clerk of the United States
District Court for the Western District of Wash-

ington, do hereby certify that the foregoing Transcript of the Record, consisting of pages numbered 1 to 71, inclusive, is a full, true and correct copy of so much of the papers and proceedings in the above entitled cause as required by Stipulation as to the Record and Praeipie to the Clerk, signed and filed on June 30, 1947, on file and of record in my office at Tacoma, Washington, and the same constitutes the Transcript of the Record on Appeal from the Judgment of the District Court of the United States for the Western District of Washington, Southern Division, to the United States Circuit Court of Appeals for the Ninth Circuit.

I do further certify that the following is a full, true and correct statement of all expenses, fees and charges earned by me in the preparation and certification of the aforesaid Transcript of the Record on Appeal, to-wit:

Appeal fee	\$ 5.00
Clerk's fee for comparing and certifying	
Record on Appeal.....	7.10
	<hr/>
	\$12.10

and I further certify that the said fees, as above set out, have been paid in full by the Appellant herein.

In Testimony Whereof I have hereunto set my hand and affixed the seal of said Court, in the City of Tacoma, Washington, this 12th day of July, 1947.

[Seal] MILLARD P. THOMAS,
Clerk.

By /s/ E. E. REDMAYNE,
Deputy.

[Endorsed]: No. 11689. United States Circuit Court of Appeals for the Ninth Circuit. Western Union Telegraph Company, a corporation, Appellant, vs. Hansen & Rowland Corporation, a corporation, Appellee. Transcript of Record. Upon Appeal from the District Court of the United States for the Western District of Washington, Southern Division.

Filed July 16, 1947.

PAUL P. O'BRIEN,
Clerk of the United States Circuit Court of Appeals
for the Ninth Circuit.

IN THE
UNITED STATES
CIRCUIT COURT OF APPEALS
FOR THE NINTH CIRCUIT

WESTERN UNION TELEGRAPH COMPANY,
a corporation, *Appellant,*

vs.

HANSEN & ROWLAND CORPORATION, a
corporation, *Appellee.*

ON APPEAL FROM THE UNITED STATES DISTRICT
COURT FOR THE WESTERN DISTRICT OF WASH-
INGTON, SOUTHERN DIVISION

BRIEF OF APPELLANT

LANE SUMMERS

Attorney for Appellant.

F. T. MERRITT

G. H. BUCEY

Of Counsel

Central Building,
Seattle 4, Washington.

PAUL P. O'BRIEN,

CLERK



IN THE
UNITED STATES
CIRCUIT COURT OF APPEALS
FOR THE NINTH CIRCUIT

WESTERN UNION TELEGRAPH COMPANY,
a corporation, *Appellant,*

vs.

HANSEN & ROWLAND CORPORATION, a
corporation, *Appellee.*

ON APPEAL FROM THE UNITED STATES DISTRICT
COURT FOR THE WESTERN DISTRICT OF WASH-
INGTON, SOUTHERN DIVISION

BRIEF OF APPELLANT

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IN THE
UNITED STATES
CIRCUIT COURT OF APPEALS
FOR THE NINTH CIRCUIT

WESTERN UNION TELEGRAPH COMPANY,
a corporation,

Appellant,

vs.

HANSEN & ROWLAND CORPORATION, a
corporation,

Appellee.

No. 11689

ON APPEAL FROM THE UNITED STATES DISTRICT
COURT FOR THE WESTERN DISTRICT OF WASH-
INGTON, SOUTHERN DIVISION

BRIEF OF APPELLANT

JURISDICTION

Jurisdiction of the trial court in this cause is based upon U.S.C. Title 28, §41 (1) conferring upon Federal District Courts original jurisdiction of all suits of a civil nature where the matter in controversy exceeds, exclusive of interest and costs, the sum of \$3000, and is between citizens of different states. In this cause the plaintiff, a Washington corporation, sued the defendant, a New York corporation, on a complaint (R. 2) to recover continually accumulating damages, alleged at a daily rate, which amounted to the sum of \$3772 when the cause was effectively commenced and to the sum of \$4920 when the cause

was removed from the State to the Federal Court, liability for which was denied by the defendant in its answer (R. 32).

Jurisdiction of the appellate court in this cause is based upon U.S.C. Title 28, §225, authorizing an appeal to a United States Circuit Court of Appeals from final decision in a Federal District Court, and upon U.S.C. Title 28, §230, requiring such an appeal to be taken within three months after entry of judgment. In this cause the judgment of the trial court (R. 61) was entered on June 2, 1947 (R. 62); and notice of appeal and supersedeas bond were duly filed on June 11, 1947 (R. 67, 68, 69; F.R.C.P. Rule 73).

ABSTRACT OF THE CASE

In this cause Hansen & Rowland Corporation as plaintiff (appellee) is seeking to recover from The Western Union Telegraph Company as defendant (appellant) statutory penalty for unlawful detainer of real property as defined by §812 of Remington's Revised Statutes of Washington.

After removal from the Superior Court of the State of Washington for the County of Pierce and after joinder of issues in the United States District Court for the Western District of Washington, Southern Division, the cause was presented for adjudication upon the complaint (R. 2), the answer (R. 32) and the stipulation of facts (R. 37) without any testimony and without a jury.

In outline the facts disclosed by the record are as follows:

- (a) At all times material the plaintiff was the owner of business premises known as 1007 Pacific Avenue in the City of Tacoma (R. 37).
- (b) At all times material to and including October 31, 1946, the defendant was tenant of said premises in lawful possession under a valid written lease (R. 37).
- (c) At all times during the currency of said lease the rent thereunder at the rate of \$325 per month was fully paid (R. 34, 38).
- (d) The defendant received the plaintiff's notice dated July 24, 1946, which ended the term of said lease as of October 31, 1946 (R. 37, 40; Ex. 1).
- (e) The defendant received from the plaintiff its unqualified notice dated September 25, 1946, to quit and surrender (R. 37, 42; Ex. 2).
- (f) The defendant orally notified the plaintiff on October 8, 1946, that the defendant was unable to vacate, whereupon the plaintiff orally advised the defendant that the sum of \$750 per month was a reasonable rental value of said premises. Thereafter, the defendant received letter from the plaintiff offering to accept payment in advance of \$1500 per month, being \$750 as "reasonable rental value" and \$750 as special damages (R. 37, 38, 43; Ex. 3).
- (g) The defendant received from the plaintiff its *alternative* notice dated November 2, 1946, to pay rent or to quit and surrender (R. 38, 45; Ex. 5).
- (h) The defendant as a public service corporation was unable to move and continued in possession after October 31, 1946, until March 7, 1947 (R. 37, 38, 40).
- (i) At all times material after October 31, 1946, the reasonable rental value of said premises was the sum of \$750 per month (R. 37, 39).

- (j) In advance, month by month, successively and cumulatively, the defendant made legal tender of rent at the rate of \$750 per month for the entire period of its occupancy after October 31, 1946,—which, in the total sum of \$3750 was duly deposited in the registry of the trial court (R. 38, 39, 44, 46, 47, 48, 49; Exs. 4, 6, 7, 8, 9).
- (k) On March 7, 1947, said premises were completely vacated by the defendant and possession thereof entirely surrendered to the plaintiff (R. 40).
- (l) As a result of the defendant's occupancy of said premises the plaintiff suffered no special damages as alleged by its complaint or otherwise (R. 38).

SPECIFICATION OF ERRORS

The appellant has specified errors (R. 73) by the trial court as follows:

1. In refusing findings of fact as proposed by the defendant (R. 53);
2. In refusing conclusions of law as proposed by the defendant (R. 53);
3. In refusing judgment as proposed by the defendant (R. 55);
4. In disregarding the defendant's disapproval of and objections to findings, conclusions and judgment as proposed by the plaintiff (R. 50, 51, 52);
5. In making findings, drawing conclusions and granting judgment as signed and filed on June 2, 1947 (R. 56-62) without hearing thereon and in the absence of attorneys for either the plaintiff or the defendant (R. 60, 62, 63).

STATEMENT OF POINTS

Appellant relies upon the following points:

1. The trial court erred in ruling that the defendant wrongfully detained said premises for the period beginning November 1, 1946, and ending March 7, 1947 (R. 60, 73);

2. The trial court erred in ruling that by reason of such unlawful detainer the plaintiff was entitled to judgment against the defendant for statutory penalty in double the amount of the reasonable rental value of said premises during said period, amounting to \$6350 (R. 60, 73);

3. The trial court erred in granting judgment for the plaintiff against the defendant in the sum of \$6350, with interest and with costs (R. 62, 73);

4. The trial court erred in granting judgment to the plaintiff which failed to exonerate the defendant except only for reasonable value of said premises at the rate of \$750 per month for said period, in the total sum of \$3175, tendered by the defendant and deposited in court (R. 61, 73).

ARGUMENT

The defendant was not guilty of unlawful detainer under Rem. Rev. Stat. §812 because the plaintiff elected to treat the defendant not as a trespasser but as a tenant.

As the result of the defendant's possession without the plaintiff's consent in the absence of agreement as to the rate of rental, the defendant became a tenant at sufferance under Rem. Rev. Stat. §10621.

The defendant as a tenant at sufferance, having duly tendered and paid the reasonable rental value of the premises, was not subject to statutory penalty in double that amount.

The factual basis for the District Court's adjudication without a jury consisted solely of the plaintiff's complaint, the defendant's answer, and the signed stipulation of facts with attached exhibits. The facts are not in dispute. Hence, on the appeal as at the trial this cause presents only questions of law.

In suing, the plaintiff invoked the statutes of the State of Washington defining and penalizing unlawful detainer of real property. So far as requiring discussion such statutes provide:

"A tenant of real property for a term less than life is guilty of unlawful detainer either—

"(1) When he holds over or continues in possession, in person or by subtenant, of the property or any part thereof after the expiration of the term for which it is let to him. In all cases where real property is leased for a specified term or period by express or implied contract, whether written or by parol, the tenancy shall be terminated without notice at the expiration of such specified term or period; or

"(3) When he continues in possession in person or by subtenant after a default in the payment of any rent, and after notice in writing requiring in the alternative the payment of the rent or the surrender of the detained premises, served (in manner hereafter in this Act provided) in behalf of the person entitled to the rent upon the person owing (owning) the same, shall have remained uncomplied with for the pe-

riod of three days after service thereof. * * *"
(Remington's Revised Statutes, §812)

"The jury, or the court if the proceedings be tried without a jury, shall also assess the damages occasioned to the plaintiff by any * * * unlawful detainer, alleged in the complaint and proved on the trial, and if the alleged unlawful detainer be after default in the payment of rent, find the amount of any rent due, and the judgment shall be rendered against the defendant guilty of * * * unlawful detainer for twice the amount of damages thus assessed and of the rent, if any, found due." (Remington's Revised Statutes, §827)

The question of law for determination: Was the defendant guilty of unlawful detainer?

Correct answer to this query requires careful consideration of the communications between the plaintiff and the defendant, as follows:

First—Notice dated September 25, 1946, from the plaintiff to the defendant "to quit and surrender" possession of the premises "at the expiration of" the defendant's "tenancy on the first day of November, 1946" (R. 42-Ex. 2).

Second—Letter dated October 8, 1946, from the plaintiff to the defendant, saying:

"Referring to your continuing in possession of the premises * * * after October 31st, 1946, please be advised that you may continue such possession for a period not exceeding four months after the expiration of the present lease on the following terms and conditions. You are to pay, in advance, rental at the rate of \$1500 per month

monthly; however, you shall have the option and privilege of vacating and surrendering up the premises at any time during the month, providing you give the owners ten days' written notice of your intention and desire so to do, and upon vacating, the unearned portion of any month's rental will be refunded to you. Conditions of space in the City of Tacoma are such that it was necessary for the owners to move one of the departments of their business to Seattle pending the time they can get possession of said premises. *They regard the premises as having a reasonable rental value of \$750 per month*, and the moving of this department to Seattle so that it could be kept intact, and employing of additional help incident to having one branch of their business done in Seattle, will cost at least \$750 per month * * *. If you desire to avail yourself of this proposal, you may do so by endorsing your acceptance hereon and returning same to writer." (R. 43-Ex. 3)

Third—Letter dated October 30, 1946, from the defendant to the plaintiff accompanying tender, saying:

"Herewith is tendered the sum of Seven Hundred and Fifty Dollars in U. S. currency, covering rental for the month of November, 1946—that amount having been claimed and demanded by your letter of October 8, 1946, as the reasonable monthly rental value of the space above mentioned, which this company is compelled by circumstances to occupy until vacation is possible." (R. 44-Ex. 4)

Fourth—Notice dated November 2, 1946, from the plaintiff to the defendant, saying:

“Please take notice that you are hereby required to pay the rental of \$1500, which became due and payable on the 1st day of November, 1946, as rental for the premises now occupied by you * * * within three days following the date of service of this notice, or in the alternative, to quit, vacate and surrender to the undersigned owners thereof possession of said premises.” (R. 45-Ex. 5)

In the background of these communications between the plaintiff and the defendant as related to the statutory definitions of unlawful detainer, the plaintiff contended, in the District Court, that the defendant was forced into one of only two possible positions, to-wit:

- A. That having impliedly accepted the offer of plaintiff's letter dated October 8th, the defendant's possession after October 31st was lawful, with accompanying obligation to pay rent in the sum of \$1500 per month; or
- B. That having rejected the offer of plaintiff's letter dated October 8th, the defendant's possession after October 31st was unlawful, with obligation for damages in the reasonable rental value of the premises being \$750 per month.

After posing these propositions the plaintiff argued in the District Court that the defendant being caught in a dilemma with only two alternatives, the court was bound to adjudge either,

- A. That the defendant, being a tenant in lawful possession but in default as to fifty per cent of the agreed rent, was liable for the unpaid balance and penalty in the sum of twice the whole rent; or

B. That the defendant, being a trespasser in unlawful possession, was liable for damages in the reasonable value of the premises and also liable for penalty in twice that amount.

In other words, the plaintiff contended below that the defendant must occupy only one of two statuses: (A) a tenant under obligation to pay any arbitrary rent demanded by the plaintiff; or (B) a trespasser under liability to pay damages.

Quite otherwise, the defendant continues to contend in the same factual background that the defendant occupied another different, intermediate status, to-wit, a tenant at sufferance—a status defined by the statutes of the State of Washington as follows:

“Whenever any person obtains possession of premises without the consent of the owner * * * he shall be deemed a tenant at sufferance merely, and shall be liable to pay reasonable rent for the actual time he occupied the premises, and shall forthwith on demand surrender his said possession to the owner * * * and all his right to possession of said premises shall terminate immediately upon said demand.” (Remington’s Revised Statutes, §10621)

This status of an occupant of real property in the State of Washington has been recognized by this court in *Klee v. U. S.*, 53 F.(2d) 58 (1931-C.C.A. 9). In this case the occupant was in possession “under a color of right” arising from a sublease which the court assumed to be “wholly invalid.” The court’s opinion said:

“Decision of this controversy hinges upon the question of whether or not the appellants were

trespassers * * *. Under the circumstances of the lease and under the Washington statute they were at least 'tenants by sufferance' and not trespassers. (§10621 quoted in full) * * *

"Furthermore, as we have seen, even if we assume that the purported sublease was wholly invalid, under the Washington law appellants would have been considered merely tenants by sufferance, and not trespassers."

Klee v. U. S., 53 F.(2d) 58, 59, 61
(C.C.A. 9).

The same recognition of the intermediate status of a tenancy at sufferance has been accorded by the Supreme Court of the State of Washington.

In *McCourtie v. Bayton*, 159 Wash. 418, an occupant was in possession of a residence a few days before the commencement of a month-to-month tenancy for which the first month's rent had been paid. During this preliminary period he was injured by the alleged negligence of a repair man employed by the owner, with resulting necessity of determining whether the occupant was a trespasser or a tenant. In holding that the occupant was a tenant by sufferance the court quoted Rem. Rev. Stat. §10621 and said:

"It is manifest that, under the foregoing statute, the landlord was protected by the legal right to recover reasonable rent for the actual time of the occupancy and the right to demand immediate possession of the premises which would terminate the right of possession at once. No such steps were taken. Therefore, even granting that no agreement had been reached as to the tenancy from February 5 to 8, there was a tenancy by sufferance."

McCourtie v. Bayton, 159 Wash. 418, 422, 423; 294 Pac. 238, 240.

In *Provident Mutual Life Insurance Co. v. Thrower*, 155 Wash. 613, the appellant had bought furniture and furnishings in a lodging house from a previous tenant and began paying some sums as rental on the real property to the agent of the respondent, a non-resident owner, without agreement having been reached as to the rate of rental as between appellant and respondent. By notice, followed by suit in unlawful detainer, the respondent claimed rent to be in arrears in the sum of \$430 at the rate of \$100 per month. The court found that appellant and respondent had never reached agreement as to the rate of the rent. In the course of the opinion, citing as authority §10621, the court said:

“If there was no meeting of minds upon the rent to be paid per month, respondent is entitled to recover upon a *quantum meruit*. *Williamson v. Hallett*, 108 Wash. 176, 182 Pac. 940; Rem. Comp. Stat. Sec. 10621.”

Provident Mutual Life Insurance Co. v. Thrower, 155 Wash. 613, 616; 285 Pac. 654, 655.

In *Williamson v. Hallett*, 108 Wash. 176, the appellant, conditional sale vendor of furniture used by the conditional sale vendee, repossessed the furniture by ousting the vendee and entering into the occupancy of the roominghouse without the consent of respondent, the landlord. The respondent as owner of the real property served notice upon appellant to quit or pay rent, and thereafter sued for unlawful detainer. In ruling as to appellant's status the court said:

“Appellant argues that, to warrant a recovery in an action of this kind, the conventional relation of landlord and tenant is indispensable and must be clearly established. Conceding this to be the law, it does not follow that such a relationship can be created only by express agreement between the parties. *Sheridan v. Doherty*, 106 Wash. 561, 181 Pac. 16. There may be and frequently is an implied contract which just as certainly creates the conventional relationship.

“‘The relation of landlord and tenant may be created by implication or by express contract. The law will, in general, imply the existence of a tenancy wherever there is an ownership of land on the one hand, and an occupation by permission on the other; for in such cases it will be presumed that the occupant intended to pay for the use of the premises. It will be implied, in many cases, where there has been no distinct agreement between the parties, or where, from various causes, the agreement may have ceased to be operative.’ 1 Taylor, Landlord and Tenant (9th ed.) §19.

“So here, as found by the trial court and established by the testimony, as we read it, although appellant entered without the knowledge or express permission of respondents, yet they immediately gave their permission by demanding the rent; and the notice to quit or pay rent in itself shows permission on their part. While we are convinced that, from the facts shown, the law will imply a tenancy and an agreement to pay rent, yet if there was no permission, the legislature has put the question at rest in this state by statute, Rem. Code, sec. 8805” (being the same as Rem. Rev. Stat. §10621, the present tenancy by sufferance statute).

Williamson v. Hallett, 108 Wash. 176, 178, 179; 182 Pac. 940, 941.

DEFENDANT'S FIRST CONTENTION

In the light of this law of the State of Washington as to tenancy at sufferance, the defendant is not liable under subsection (1) of Rem. Rev. Stat. §812 for unlawful detainer penalty on the facts in this case.

Because of the plaintiff's notice dated July 24th the life of the lease according to its terms was definitely ended on October 31st. Plaintiff's absolute notice to "quit *and* surrender," dated September 25th (R. 42-Ex. 2) although possibly psychologically expedient was certainly legally superfluous, Rem. Rev. Stat. §812(1). In any event, before subsequent negotiations between the plaintiff and the defendant, and before subsequent notices from the plaintiff to the defendant, the plaintiff had unqualified right to treat the defendant as a trespasser if it continued in possession after October 31st.

But before commencing this action the plaintiff waived such right to proceed against the defendant as a trespasser.

Plaintiff (after having offered on October 8th to permit the defendant to continue as a tenant in lawful possession upon advance payment of \$1500 per month, and after having received on October 30th defendant's tender of \$750 for November) elected to treat the defendant as a tenant by plaintiff's notice dated November 2nd (R. 45-Ex. 5) wherein plaintiff declared rent "became due and payable on the first

day of November, 1946," and granted defendant the option *either* "to pay" or "to quit."

In this legal conclusion the defendant is supported by the express language and the plain purpose of the plaintiff's notice dated November 2nd, and also by the already quoted opinion of the Washington Supreme Court construing the legal effect of similar alternative notice, wherein that court said

"* * * the notice to quit or pay rent in *itself* shows permission on their (the landlords') part."

Williamson v. Hallett, 108 Wash. 176, 179;
182 Pac. 940, 941.

Hence, the unlawful possession of the defendant, obtaining on November 1st, was converted by the plaintiff itself on November 2nd into the lawful possession of the defendant, which so remained thereafter, since the plaintiff never at any time served upon the defendant later notice of any kind to alter the same. In other words, the plaintiff changed the defendant's status of trespasser as existing on November 1st into the defendant's status of tenant at sufferance as existing at all times after November 2nd.

Therefore, on the date the plaintiff subsequently instituted this cause the defendant was a tenant at sufferance. On that date the defendant was not (to paraphrase subsection (1) Rem. Rev. Stat. §812) "holding or continuing in possession after the expiration of the term for which let to the defendant under the original lease terminated as of October 31st."

To conclude discussion respecting subsection (1) of

Rem. Rev. Stat. §812, that subsection not being applicable to the defendant or its possession when the action was begun, the defendant was not guilty of unlawful detainer thereunder, and is not now liable for penalty thereunder.

DEFENDANT'S SECOND CONTENTION

In the light of the law of the State of Washington as to tenancy at sufferance, established by the statute (Rem. Rev. Stat. §10621) and the decisions heretofore reviewed, the defendant is not liable for unlawful detainer penalty under subsection (3) of Rem. Rev. Stat. §812.

By its letter of October 8th (R. 43, Ex. 3) the plaintiff proposed that the defendant after October 31st continue in lawful possession of the premises on condition that the defendant pay in advance the sum of \$1500 per month. The defendant never accepted this offer. However, the defendant did consider this offer from October 8th until October 30th.

The plaintiff's letter of October 8th made two important assertions: first, that the premises had a "reasonable rental value of \$750 per month"; second, that the plaintiff would have "to move one of the departments" of its business to Seattle with resulting "cost at least \$750 per month" to the plaintiff during the defendant's continued occupancy. Having failed to secure another renewal of its lease — already several times previously extended (R. 57) — and being unable to disrupt its public service by vacation of the premises on October 31st, the defendant's consideration of the plaintiff's offer developed several conclu-

sions: (a) that the plaintiff would actually suffer no special damages as claimed in the sum of \$750 or any other sum; (b) that \$750 per month was a high figure as representing the reasonable rental value of the premises; (c) that the defendant must tender and pay whatever amount was the actual reasonable rental; and (d) that if the defendant did tender and pay the sum of \$750 per month, which the plaintiff itself set as the reasonable value, then unlawful detainer penalty could not be legally awarded.

So motivated, on October 30th the defendant replied to the plaintiff's offer with a legal tender of \$750—"that amount having been claimed and demanded" by the plaintiff "as the reasonable monthly rental of the space" (R. 44, Ex. 4).

However, the plaintiff by its letter of October 8th had demanded an arbitrary, exorbitant rent in the sum of \$1500, being expressly based upon \$750 claimed as reasonable rental value plus \$750 claimed as special damages—the excessive quality of plaintiff's demand in the sum of \$1500 now being settled in this cause by the stipulation of facts, which recites in paragraph 7 (R. 38) "that the plaintiff suffered no special damages as alleged by its complaint or otherwise, and is not entitled to recovery thereof."

Because plaintiff's demand for \$1500 was extortionate it was not accepted by the defendant. The blank endorsement for acceptance at the bottom of plaintiff's letter of October 8th was never signed by the defendant as requested therein (R. 44, Ex. 3). The defendant's tender of \$750 on October 30th was an

affirmative rejection of the plaintiff's demand for \$1500 to the extent of half that amount (R. 44, Ex. 4).

Since the defendant never accepted the plaintiff's demand at the rate of \$1500 and the plaintiff never accepted the defendant's tender at the rate of \$750, it necessarily follows that on November 1st the plaintiff was not consenting to the defendant's possession as then obtaining, and that after November 1st there was nothing but disagreement between the plaintiff and the defendant as to the amount of rent to be paid and received for the premises.

Nevertheless, on November 2nd, with no agreement about the rate of rent, the plaintiff elected to treat the defendant not as a trespasser but as a tenant, by serving plaintiff's notice, which gave to the defendant the option either "to pay" or "to quit" (R. 45-Ex. 5). As a matter of law, already demonstrated, this notice of November 2nd converted unlawful possession obtaining on November 1st into lawful possession at all times thereafter — the possession of a statutory tenant at sufferance. But, plaintiff's notice of November 2nd neither changed disagreement as to the rate of rent into agreement nor modified the defendant's obligation therefor. Being a tenant at sufferance, the defendant was bound by statute only "to pay reasonable rent for the actual time" it "occupied the premises" (Rem. Rev. Stat. §10621).

Such was the defendant's status on the later date when the plaintiff initiated this cause. On that date the defendant was not (to paraphrase subsection (3)

Rem. Rev. Stat. §812) "continuing in possession after a default in the payment of any rent" because the plaintiff and the defendant had no contract, express or implied, as to rent in any specific amount, and because the defendant had already tendered all rent due in the sum of \$750 representing the reasonable rental value of the premises as then claimed by the plaintiff (R. 43-Ex. 3) and as since stipulated of record (R. 39).

To conclude discussion respecting subsection (3) of Rem. Rev. Stat. §812, that subsection not being applicable to the defendant or its possession when this cause was begun, the defendant was not guilty of unlawful detainer thereunder, and is not now liable for penalty thereunder because of its successive, cumulative tenders timely made and also timely perpetuated by deposits in court.

CONCLUSION

In conclusion, the defendant contends in this cause upon the undisputed facts there being no unlawful detainer established as defined by any applicable subsection of Rem. Rev. Stat. §812, the judgment of the District Court should have been in favor of the defendant and against the plaintiff to the extent and to the effect that the plaintiff take, but take only, from the defendant's tenders on deposit the sum of \$3175, being the reasonable rental at the rate of \$750 per month for the period beginning November 1, 1946, and ending March 7, 1947, that being "the actual time it occupied the premises" (Rem. Rev. Stat. §10621). Otherwise stated, the defendant contends that on the

facts in this cause the plaintiff was not entitled to judgment in its favor in excess of the amount conceded, and, hence, was not entitled to any penalty under Rem. Rev. Stat. §827.

Finally the defendant contends that this court should now reverse the judgment of the District Court, with mandate directing the return to the defendant of the residue of its deposit in the sum of \$575 and allowing to the defendant its costs and disbursements.

Respectfully submitted,

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In the
United States
Circuit Court of Appeals
FOR THE NINTH CIRCUIT

No. 11689

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PANY, a corporation,

Appellant,

vs.

HANSEN & ROWLAND CORPORATION,
a corporation,

Appellee.

FOR THE WESTERN DISTRICT OF WASHINGTON,
ON APPEAL FROM THE UNITED STATES DISTRICT COURT
SOUTHERN DIVISION

HONORABLE CHARLES H. LEAVY, *Judge*

BRIEF OF APPELLEE

CHARLES T. PETERSON
PETERSON & DUNCAN
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Tacoma, Washington

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§10620 -----	9
§827 -----	19, 20
Pierce's 1943 Code	
§55-5 -----	8
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PC7970 -----	12

OTHER AUTHORITIES

19 Am. Jurisprudence 730-733-----	13
24 Cyc. p. 1168-----	14
Sedgwick on Damages (9th Ed.) §99e-----	18
Tiffany, Landlord & Tenant, Vol. 2, p. 1493 -----	14, 15, 21

In the
United States
Circuit Court of Appeals
FOR THE NINTH CIRCUIT

No. 11689

WESTERN UNION TELEGRAPH COM-
PANY, a corporation,

Appellant,

vs.

HANSEN & ROWLAND CORPORATION,
a corporation,

Appellee.

FOR THE WESTERN DISTRICT OF WASHINGTON,
ON APPEAL FROM THE UNITED STATES DISTRICT COURT
SOUTHERN DIVISION

HONORABLE CHARLES H. LEAVY, *Judge*

BRIEF OF APPELLEE

JURISDICTION

Jurisdiction of this court on this appeal is conceded for the reasons set forth in Appellant's brief.

STATEMENT OF CASE

We think a more complete statement of the issues made by the pleadings and of the facts than made by Appellant may be helpful to the Court, and rather than attempt the difficult task of supplement-

ing Appellant's abstract we will endeavor to restate the case.

As disclosed by the record, on December 2nd, 1932, the premises in question were leased by Appellant for a period of six years, which lease contained among others the following provision :

“Unless either party hereto shall give to the other at least three months prior to the end of said term written notice of his or its desire and intent to terminate this lease at the end of said term, this lease shall continue upon the terms and conditions then in force for a further period of one year and so on from year to year until terminated by either party hereto giving to the other written notice at least three months prior to the expiration of the then current term of his or its desire and intent to terminate this lease at the end of said term.”

During the month of May, 1938, the lease was extended by agreement in writing for a period of three years from the 1st day of November, 1938. The provision above set forth in the original lease was by said agreement continued in force, and thereafter on February 27th, 1941, the lease was again extended by agreement in writing for an additional period of five years, ending on the 1st day of November, 1946, and said provision above set forth as again incorporated in the extension agreement.

(Par. III Complaint Tr. P. 4-5) admitted by Answer (Tr. p. 32). The last extension was at an annual rental of \$3900.00 payable in monthly installments of \$325.00 per month. On July 24th,

1946, Appellee gave Appellant the written notice above provided terminating said lease in accordance with its terms, as of October 31, 1946 (Ex 1, Tr. 40) which was supplemented (probably superfluous) by a further notice as follows:

NOTICE

TO:

Western Union Telegraph Company
Tenants in possession of premises at
1007 Pacific Avenue
Tacoma, Washington

Please Take Notice that the undersigned owner of the following described real property in Pierce County, Washington, to-wit:

Lot Four (4) in Block One Thousand Three
(1003) Map of New Tacoma, W. T., in
Pierce County, Washington,

commonly known as House No. 1007 Pacific Avenue in the City of Tacoma, Washington, hereby notifies you that you are hereby required to quit and surrender up to the undersigned owner entitled thereto the possession of the above-entitled premises now occupied by you as tenant, at the expiration of your tenancy on the first day of November, 1946.

Dated at Tacoma, Washington, September 25th, 1946.

HANSEN & ROWLAND CORPORATION,

By Charles T. Peterson,
Agent and Attorney.

(Ex 2 p. 42 Tr.)

In a discussion of the matter on October 8th, 1946, Appellant orally notified Appellee that it

would be unable to vacate the premises on October 31st, 1946. Appellee by letter confirmed an oral proposal to Appellant to extend the term as follows:

Tacoma, Washington
October 8, 1946

Western Union Telegraph Company
1007 Pacific Avenue
Tacoma, Washington

Attention: Mr. R. H. Cobb

Gentlemen:

Referring to your continuing in possession of the premises at 1007 Pacific Avenue, Tacoma, Washington, after October 31st, 1946, please be advised that you may continue such possession for a period not exceeding four months after the expiration of the present lease on the following terms and conditions.

You are to pay, in advance, rental at the rate of \$1500 per month, monthly; however, you shall have the option and privilege of vacating and surrendering up the premises at any time during the month, providing you give the owners ten days' written notice of your intention and desire so to do, and upon vacating, the unearned portion of any month's rental will be refunded to you.

Conditions of space in the City of Tacoma are such that it was necessary for the owners to move one of the departments of their business to Seattle pending the time they can get possession of said premises. They regard the premises as having a reasonable rental value of \$750.00 per month and the moving of this department to Seattle so that it may be kept intact, and employing of additional help incident to having one branch of their business done in Seattle, will cost at least \$750.00 per month, and

undoubtedly, considering the cost of moving, more than that amount.

If you desire to avail yourself of this proposal, you may do so by endorsing your acceptance hereon and returning same to writer.

HANSEN & ROWLAND, INC.,

By Charles T. Peterson,
Agent and Attorney.

We hereby accept and agree to the foregoing:
WESTERN UNION TELEGRAPH COMPANY,

By-----

(Tr. 37-43-4)

On October 30, 1946, Appellant addressed a letter to Appellee as follows:

Hansen & Rowland Corporation
Hansen & Rowland, Inc.
Tacoma, Washington

Gentlemen:

Re: 1007 Pacific Avenue - Western Union
Telegraph Company office space

Herewith is tendered the sum of Seven Hundred and Fifty Dollars in U. S. currency, covering rental for the month of November, 1946—that amount having been claimed and demanded by your letter of October 8, 1946, as the reasonable monthly rental value of the space above mentioned, which this company is compelled by circumstances to occupy until vacation is possible.

Yours very truly,

WESTERN UNION TELEGRAPH COMPANY,
By MERRITT, SUMMERS & BUCEY,
Its Attorneys.

LS/ley
(Ex 4; Tr. 44)

On November 2nd, 1946, Appellee served notice on Appellant as follows:

NOTICE

To: Western Union Telegraph Company, Tenants in possession of premises at 1007 Pacific Avenue, Tacoma, Washington

Please take notice that you are hereby required to pay the rental of \$1500.00, which became due and payable on the 1st day of November, 1946, as rental for the premises now occupied by you, to-wit:

Lot Four (4) in Block One Thousand Three (1003) Map of New Tacoma, W. T., in Pierce County, Washington,

commonly known as house No. 1007 Pacific Avenue in the City of Tacoma, Washington, within three days following the date of service of this notice, or in the alternative, to quit, vacate and surrender up to the undersigned owners thereof possession of said premises.

Please govern yourself accordingly.

Dated at Tacoma, Washington, November 2, 1946.

HANSEN & ROWLAND CORPORATION,

By Charles T. Peterson,

Its Agent and Attorney.

(Ex 5; Tr. p. 45-6)

which notice remained uncomplied with. That each month thereafter Appellant made tenders to Appellee of \$750.00 per month and kept same good by paying the amount into Court.

Appellee desired Appellant to vacate said

premises to permit remodeling of same (Appellant's Answer, Tr. 35).

It was stipulated (10 Tr. 39), and the Court found as a fact that the reasonable rental value of the premises, at all times material, was \$750.00 per month. (Finding 11, Tr. 59). Upon trial of the case the lower court adjudged Appellant guilty of unlawful detainer of the premises and allowed damages in the amount of \$750.00 per month, and assessed the penalty in a like amount as provided by the Washington Statute, from which judgment this appeal is prosecuted.

ARGUMENT

Appellant contends that it was not guilty of unlawful detainer, tacitly conceding that if it were Appellee became entitled to the rental value of the premises plus the penalty in like amount, but takes the position that its wrongful holding over after the term constituted "Obtaining the possession of premises without the consent of the owner" and therefore it became a tenant by sufferance under the Washington Statutes, and liable only for reasonable use value. (Brf. pp. 5-6).

It is important here to consider the pertinent Washington Statutes. The unlawful detainer statute provides:

"Unlawful Detainer Defined. A tenant of real property for a term less than life is guilty of unlawful detainer either (1) when he holds

over or continues in possession, in person or by subtenant, of the property or any part thereof after the expiration of the term for which it is let to him. In all cases where real property is leased for a specified term or period by express or implied contract, whether written or by parole, the tenancy shall be terminated without notice at the expiration of such specified term or period; * * * (3) When he continues in possession in person or by subtenant after a default in the payment of any rent, and after notice in writing requiring in the alternative the payment of the rent or the surrender of the detained premises, served (in manner hereafter in this act provided) in behalf of the person entitled to the rent upon the person owning the same, shall have remained uncomplied with for the period of three days after service thereof. * * * (6) Any person who shall, without the permission of the owner and without having any color of title thereto, enter upon the land of another, and who shall fail or refuse to remove therefrom after three days notice, in writing, to be served in the manner provided in this act. O5p173 PC7970 RRS812."

(Sec. 55-5 Pierce's 1943 Code; R.R.S. Sec. 812)
The statute defining Tenancy by sufferance provides:

"Tenant by Sufferance. §2057-5. Whenever any person obtains possession of premises without the consent of the owner or other person having the right to give said possession, he shall be deemed a tenant by sufferance merely, and shall be liable to pay reasonable rent for the actual time he occupied the premises, and shall forthwith on demand surrender his said possession to the owner or person who had the right of possession before said entry, and all his right to possession of said premises shall terminate

immediately upon said demand. PC3556 RRS 10621." (Sec. 719-7 Pierce's 1943 Code; R. R. S. 10621).

"Tenancy for Specified Time. §2055-3. In all cases where premises are rented for a specified time by express or implied contract, the tenancy shall be deemed terminated at the end of such specified time. PC3555 RRS10620." (Sec. 719-5 Pierce's 1943 Code; R.R.S. 10620).

It will be seen that to constitute an unlawful detainer, as applied to this case, the facts must meet any one or more of the following tests:

- (a) Where premises are leased for a term less than life, a holding over by the tenant after expiration of the term; or
- (b) Where premises are rented with monthly rent reserved and tenant defaults in payment of rent and continues in possession after being given three days' notice to pay rent, or in the alternative to surrender possession of the premises; or
- (c) In cases where one without permission of owner and without color of title thereto enters upon lands of another and fails to remove therefrom after three days notice in writing.

To constitute a tenancy by sufferance two conditions must be present:

- (a) Obtaining possession of premises without the consent of the owner; and

- (b) Absence of a demand on the part of the owner for a surrender of possession.

Neither condition is present here. Appellant was let into peaceful possession of the premises by the owner under a valid lease. The statutory written demand was made on Appellant for surrender of possession, which demand was refused.

Approaching the case from any view point it is obvious that Appellant's status answers the tests of the unlawful detainer statute. The fact that prior to the expiration of the term a discussion was had looking to the extension of the term, or the making of a new lease on different terms could not, and did not, operate to terminate the status of Appellant, who was let into possession of the premises for a term by express consent of the owner and held over after expiration of the term, and convert it into a tenancy by sufferance, defined by statute as a status created whenever any person obtains possession of premises without the consent of the owner and retains such possession only in the absence of a demand by the owner to surrender same.

Counsel for Appellant advances a rather ingenious argument to sustain their theory that Appellant was a tenant by sufferance, contending in substance that such relationship arose,

“As the result of the defendant's possession without the plaintiff's consent in the absence of agreement as to the rate of rental, the de-

fendant became a tenant at sufferance under Rem. Rev. Stat. § 10621.”
(P. 5 Appellant’s Brief).

To follow this contention to its logical end would result in abrogating the unlawful detainer statutes of the state. It would open the way for any tenant wrongfully holding over after the expiration of his term to discuss the terms of a new lease with his landlord and, not agreeing, continue his wrongful holding over, freed of the penalty imposed by statute. In their zeal in pursuit of this illogical theory counsel apparently lost sight of that part of the Tenancy by Sufferance Statute which provides: The tenant

“ * * * shall forthwith on demand surrender his said possession to the owner or person who had the right of possession before said entry, and all his right to possession of said premises shall terminate immediately upon said demand.”

Conceding for argument’s sake that a tenancy by sufferance came into existence on November 1st, 1946, the three-day written notice served on Appellant on November 2nd, (Ex 5, Tr. 45) demanding payment of the rental of \$1500.00, or in the alternative surrender the premises was a sufficient demand for surrender of possession under the Tenancy by Sufferance Statute, and Appellant’s failure to heed the Notice brought into operation Section 6 of the unlawful detainer statute, which provides:

“ * * * (6) Any person who shall, without the permission of the owner and without having any color of title thereto, enter upon the

land of another, and who shall fail or refuse to remove therefrom after three days notice, in writing, to be served in the manner provided in this act. O5p173 PC7970 RRS812.”

The stark naked controlling facts of the case are that the owner desired possession of the premises at the end of the five-year term expiring on October 31, 1946, and on July 24th, 1946 gave the tenant (Appellant) timely notice of termination of the lease. On October 8th owner discussed with and proposed the terms of an extension or new lease with tenant, confirmed by letter on the same date, stating the terms of such extension or new lease acceptable to owner. The owner's proposal was not expressly accepted by tenant, who made a counter proposal on its own terms (implied by its tender of a certain amount as rent) not acceptable to owner, whereupon tenant elected at its risk to hold over.

Applying the statute law of the State of Washington to the above facts the Court had no alternative but to find Appellant guilty of unlawful detainer.

ESTOPPEL

Appellant by answer sought to plead an estoppel, alleging in substance that it was a public service corporation engaged in a world wide telephone and telegraph business; that the premises in question were an integral part of its system, and that by reason of conditions beyond its control it was unable to vacate the premises, and that the owner intended upon its vacating said premises to remodel the same

and had received a permit from the Civilian Production Administration of the United States, granted only upon condition that Appellant's service to the public be protected and that the work of remodeling be not commenced before December 1, 1946 (Par. 10-11 Answer, Tr. 35-6), and while not particularly arguing the matter in its brief, it advances the fact that it was impossible for it to move at the expiration of the term.

The Supreme Court of the State of Washington is committed to the rule that an estoppel will not lie in an unlawful detainer case. *Morse vs. Healy Lumber Company* 33 Wash. 451, 74 Pac. 662; *Armstrong vs. Burkett*, 104 Wash., 476; 177 Pac. 333. The facts alleged are insufficient to constitute an estoppel in that they lack the essential elements of estoppel, particularly in that there is no claim that Appellant was led to its prejudice in a belief and reliance on conditions created by the owner (19 Am. Jurisprudence pp. 730-733).

PLAINTIFF'S ACTION

Appellant contends that the unlawful detainer statute does not apply because plaintiff elected to treat defendant not as a trespasser but as a tenant (Appellant's Brief, p. 5). On October 8th, 1946, owner notified tenant in writing that it could continue to occupy the premises after October 31, 1946 upon paying advance rental at the rate of \$1500.00 per month, and requested tenant, if it desired to

avail itself of the proposal, to endorse its acceptance on the writing (Ex. 3 Tr. 43). Tenant did neither and refused to become a lawful tenant but continued in wrongful possession of the premises. It was plaintiff's contention in the lower court, and its action was brought on the theory that after tenant received definite notice of an increase in rent seasonably given during the term, to become effective at the expiration of the term, and notwithstanding tenant protested the increase and held over beyond the term, that such holding over constituted an implied acceptance of the proposal.

The court in *Commercial Cable Co. vs. McKenna*, 168 NYS 13, in which the facts as stated by the court practically parallel the facts here, sustained such contention. The principle is stated in 24 Cyc. p. 1168, as being supported by the great weight of authority. See also *Tiffany, Landlord and Tenant*, Vol. 2, p. 1493; *Steas vs. Bergmeier* (Minn.) 98 N.W. 648; *Moore vs. Harter* 65 N.E., 883.

We think the lower court erroneously rejected this contention, and while appellee has not appealed from the court's action in this respect, it explains appellee's reason for giving the notice of November 2nd, 1946 demanding rental of \$1500.00 per month or in the alternative surrender of the premises, the rejection of which by appellant resulted in the bringing of this action.

HOLDING OVER

The fact that it was inconvenient or, as counsel

says, impossible for Appellant to vacate the premises at the expiration of the term is no defense. *Morse vs. Healy Lumber Company*, supra: *Armstrong vs. Burkett*, supra. The rule is stated by the author of *Tiffany, Landlord and Tenant*, Third Edition, page 1498, as follows:

“The holding over is not other than willful, because the tenant cannot vacate without great inconvenience and injury to his business.”

There would be but little virtue in the forcible entry or unlawful detainer statutes if their manifest purpose could be defeated by a party wrongfully taking or withholding possession of premises and justify his conduct by pleading hardship, inconvenience or inability to vacate and surrender up to one lawfully entitled to possession. It might well be that in such a case the owner having all the equities in his favor, would suffer a greater loss than the offending tenant.

MEASURE OF RECOVERY—DOUBLE THE RENTAL VALUE

Under the stipulated facts, it was agreed that at all times material the reasonable rental value of the premises was \$750.00 per month (Tr. 39; Finding Tr. 54), and it is a fact that the rental for the premises during the five-year extension of the lease expiring on October 31, 1946, was \$3900.00 per annum, payable in monthly installments of \$325.00 each. The Supreme Court of the State of Washington is unqualifiedly committed to the rule that the

reasonable rental value at the time is the measure of recovery.

In the case of *Owens vs. Layton*, 133 Wash., 346, 233 Pac. 645, the Court had occasion to mark the distinction between those cases where a tenant in possession under a valid lease presently in force fails to pay the rent reserved and those cases where the premises are wrongfully held by a former tenant whose lease has expired. In the first situation the damage will be twice the amount of the reserved rent, as provided in the lease. In the second situation, (which applies to the instant case), the measure of damages will be twice the amount of the fair market rental value of the property. In the course of its opinion the court said:

“The sole question on the appeal arises on the following instruction, which is complained of by the appellants:

“ ‘The measure of damages will be the fair market rental value of the property. The burden is on the plaintiff to show and prove damages by a preponderance of the evidence. Whatever the preponderance of the evidence shows will be the fair rental value of the property,—fair rental market value of the property during the time it has been retained, if it has been retained, that would be the amount of damages you would award the plaintiff in your verdict.’

“In effect, the argument on behalf of the appellants is that the ‘statute makes a distinction between the rent falling due during the period the premises are unlawfully detained and special damages which might accrue dur-

ing that period; that, in the present case, the appellants held over for two months after the termination of their tenancy by a notice to quit, entitling the jury to find a verdict for rent due in the sum of \$200, the agreement being \$100 per month; and that there was no proof introduced tending to show special damages.'

"The contention misconceives the true situation in important particulars. After November 30, 1923, no rent became due. Rent is an incident of a tenancy, and on that date, as appellants admit or say, the tenancy terminated by the notice to quit that had been given. Thereafter the appellants in holding the premises were trespassers and liable for general damages, not determinable by the rate theretofore paid as rent, but by the market rental value of the premises during the time of trespass."

To the same effect is *Lee v. Debentures Incorporated*, 8 Wash. 2nd, 353, 112 Pac. 2nd, 142; *Sunday v. Moore*, 135 Wash., 414; 237 Pac. 1014; *Reichlin v. First National Bank*, 184 Wash., 304; 51 Pac. 2nd 380.

THE STATUTE AS TO THE PENALTY IS MANDATORY

The court has no discretion in the matter. Neither does a tender and payment into court of an amount equal to the reasonable rental value excuse the enforcement of the statute. In *Armstrong v. Burkett*, 104 Wash., 476, 177 Pac. 333, the court said:

"Counsel bitterly complains that, having tendered and paid into court the rent from August 15 up to the time of the trial, being for the intervening time, the court should not visit the

penalty of the statute upon his client. Our heart is with him and with his client, but the statute Rem. Code § 827, must guide our hand. It leaves no legitimate ground for the exercise of our sympathy. The trial judge had no discretion, nor have we. *Newman v. Worthen*, 57 Wash. 467, 107 Pac. 188; *Bond v. Chapman*, 34 Wash. 606, 76 Pac. 97; *O'Connell v. Arai*, 63 Wash. 280, 115 Pac. 95; *Shannon v. Loeb*, 65 Wash. 640, 118 Pac. 823.

"It is no answer to say that plaintiffs might have withdrawn the money as it was paid in. A suit pending, it is likely that an acceptance of the amount tendered would have satisfied counsel's theory, a hazard plaintiffs were not called upon to take. It was their privilege to fix the legal rights of the parties as of the day of forfeiture."

In *Reichlin vs. First National Bank*, 184 Wash., 304, the court said:

" * * * The value of the use and occupancy therefore, was, under what seems to be the universal rule, the sole measure of damages. The value of the use and occupancy and the fair rental value seem to be one and the same thing, and under the issues submitted to the jury, no verdict could be properly returned save one based upon that measure.

"3 Sedgwick on Damages (9th ed.) § 99e, gives the rule as follows:

" 'Where one occupies land of another without an express covenant to pay rent, the owner may recover the rental value of the land in an action for use and occupation. The rental value is the actual value for profitable use, not the value of the use which the owner meant to make of it.' "

(Op. 311) Citing the case of *Owens v. Layton*, *supra*.

In *Davis v. Jones*, 15 Wash. 2nd, 572, 131 Pac. 2nd, 430, the Court had occasion to again consider the effect of tender and payment into court, in which case it reiterated, in substance, the statement in the *Armstrong* case, saying:

“ * * * Defendant also tendered and paid into court the rent from date of termination of her tenancy to the time of trial of the action. She argued that by reason of that tender and payment into court that the penalty of the statute (Rem. Rev. Stat. § 827)—judgment for double the amount of rent accrued—should not be visited upon her. We held that while our heart was with appellant we must be guided by the statute (Rem. Rev. Stat. § 827) which left no legitimate ground for the exercise of our sympathy; that the trial court was without discretion, as were we.”

(Op. 579).

The following additional cases may be consulted:

Lowman vs. Russell, 133 Wash. 10, 233 Pac. 9; *McDuffie v. Noonan*, 176 Wash. 436, 29 Pac. 2nd 684.

Measure of damages and penalty.

Fisher Executor v. Clark, 98 Wash. 382, 167, Pac. 1103.

Hinckley v. Casey, 45 Wash. 430, 88 Pac. 753, where it was contended that the court may double the damages in unlawful detainer cases only where the action is brought for the nonpayment of rent. The Court (Justice Rudkin) said:

“ * * * The penalty is not imposed for the nonpayment of rent, as the defendants suggest. If it were, the act could not be sustained on constitutional grounds. The penalty is imposed for the refusal to surrender possession on the termination of the tenancy, whether it be terminated by the terms of the lease, for nonpayment of rent, or for any of the other causes specified in the statute. The question is not a new one in this court. Double damages were allowed in *Hart v. Pratt*, 19 Wash. 560, 53 Pac. 711; *Quandt v. Smith*, 28 Wash. 664, 69 Pac. 369, and *Bond v. Chapman*, supra. Each of these actions was for an unlawful detainer, and in neither case was the tenancy terminated for the nonpayment of rent.

“The judgment is reversed and the case remanded with direction to enter judgment for double damages as prayed in the complaint.”

Followed in *Swanson v. Stubb*, 108 Wash., 170, 183 Pac. 91, where the Court (Fullerton) said:

“ * * * The exception noted is the contention that the court erred in entering judgment for twice the amount of the damages returned by the jury. It is argued that the statute (Rem. Code, § 827) permits such doubling only in cases where the verdict of the jury is founded on nonpayment of rent. But the question does not require discussion. It was met and determined by this court contrary to this contention in the case of *Hinckley v. Casey*, 45 Wash. 430, 88 Pac. 753.”

(Op. 173).

Bond v. Chapman, 34 Wash. 606, 76 Pac. 97, where the court held that it was not competent to interpose an equitable defense in an unlawful de-

tainer action. That the penalty statute was so plain that it was not susceptible of construction.

O'Connell v. Arai, 63 Wash. 280, 115 Pac. 95 (En Banc) holding penalty statute mandatory, and quoting with approval from *Hinckley v. Casey*, *supra*.

In discussing the purpose of a statute imposing a penalty for holding over, the Author of *Tiffany, Landlord and Tenant*, Third Edition, page 1498, says:

“The purpose and effect of the rule appear to be to impose a penalty upon the tenant wrongfully holding over, and this penalty it adjusts without reference to the actual wrong inflicted upon the landlord as measured by the period of the holding over, or to the culpability of the tenant.”

CASES CITED BY APPELLANT

In support of its contention that appellant was a tenant by sufferance, counsel cite *Klee v. U. S.*, 53 Fed. (2d) 58, a criminal prosecution for liquor law violation. The decision of the case hinged upon the question of whether or not defendant, who was in possession of the premises was a trespasser, which status would preclude him from claiming the benefit of the Fourth Amendment with respect to searches and seizures. According to the facts stated, the officers sought to justify their entry of the premises by the terms of lease given by the proprietor of a farm to one Hill. Proprietor died and it was claimed his

executor gave the Federal officers permission to enter the premises for the purpose of searching. The lease contained a provision against assignability without the consent of the proprietor, and the executor denied having given any consent. On the other hand, defendants claim they were occupying the dwelling under a subletting from Hill and denied the authority of the executor to give anyone the right to enter and search the premises. We have read and re-read the case with care and it does not appear to us there is anything contained in the opinion that has any bearing on the questions involved in this case.

McCourtie v. Bayton, 159 Wash. 418 (page 11 Appellant's Brief). Action for damages by child of tenant suffering injuries as result of defect in premises. The facts show that tenant, with consent of Agent or landlord entered possession of premises pursuant to agreement of lease, but two or three days prior to effective date of lease. The tenancy by sufferance statute was only referred to incidentally. Clearly, the case is not an authority here.

Provident Mutual Life Insurance Company vs. Thrower, 155 Wash. 613, involved a dispute as to whether or not any rent was agreed upon between the parties. After occupant had been in possession of premises for a period, agent of landlord served notice on occupant claiming rent at the rate of \$100.00 per month. Since the jury found by its verdict that there was no agreement as to rent, the court held that recovery could be had on *quantum meruit*.

We do not understand on what theory the case may be regarded as an authority here. In the Provident case the owner consented to the occupancy of the premises by the tenant without any agreement as to rent, as the jury found. The action was for past due rent. In the instant case the owner notified defendant before any rent accrued that the rental would be \$1500.00 per month, as it had a right to do, and upon failure to pay it promptly demanded payment or, in the alternative, the surrender up of possession of the premises, neither of which demands were complied with by the tenant, whose occupancy thereafter was without the consent of the landlord.

The case of *Williamson v. Hallett*, 108 Wash. 176 (Appellant's Brief p. 12), held that where one entered premises without owner's consent and owner thereafter demanded rent and occupant continued in possession of premises, the relationship of landlord and tenant was created by implication. The court held that an unlawful detainer action on the facts stated could be maintained, and referred only to the tenancy by sufferance statute incidentally, it being the defendant's contention that she never was in possession of the premises.

CONCLUSION

It is crystal clear that Appellee's action on the liability of Appellant rests entirely on the status of the parties created by the making of the original lease back in 1932, the terms of which were extended to October 31st, 1946, when it terminated. Under

the terms of this lease Appellant went into lawful possession of the property, which lawful possession continued until and including the 31st day of October, 1946. It is unimportant and immaterial that Appellee offered to extend the lease for a period at the rental of \$1500.00 per month, which Appellant did not expressly accept or reject, but held over and attempted to exercise the prerogatives of the owner and fix the rent of its property at \$750.00 per month by tendering that amount, which tender the owner refused. Since such holding over by the tenant was without the consent of the owner, the tenant became liable for the reasonable rental value plus the penalty provided by statute. In the final analysis of the matter the decision of this case turns on the question of consent by the owner. The record makes it perfectly clear that the only consent to continue occupancy by the tenant was conditioned on the payment by the tenant of \$1500.00 per month rental. Holding over without the consent of the owner, under the unlawful detainer statute, made the tenant liable for the amount of the judgment awarded by the trial court. Assuming that the tenancy by sufferance statute has any place in the case, we have the demand for surrender up of possession of the premises made on November 2, 1946 uncomplished, which brings the case within Section 6 of the unlawful detainer statute and subjects tenant to the same liability. It appears to us that the appeal in this case is so devoid of merit, and is so strongly impressed with the ap-

pearance of having been sued out merely for delay, that this court should award additional damages at a rate not exceeding 10%, in addition to interest, as provided by Rule 26 of this court.

Respectfully submitted,

CHARLES T. PETERSON
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Attorneys for Appellee

520 Perkins Building
Tacoma 2, Washington



11680
No. 11689

IN THE
UNITED STATES
CIRCUIT COURT OF APPEALS
FOR THE NINTH CIRCUIT

WESTERN UNION TELEGRAPH COMPANY, a corporation
Appellant,
vs.
HANSEN & ROWLAND CORPORATION, a corporation,
Appellee.

ON APPEAL FROM THE UNITED STATES DISTRICT
COURT FOR THE WESTERN DISTRICT OF
WASHINGTON, SOUTHERN DIVISION

APPELLANT'S REPLY BRIEF

LANE SUMMERS,
Attorney for Appellant.

F. T. MERRITT,
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Of Counsel.

Central Building,
Seattle 4, Washington.

FILED

OCT 14 1947

PAUL P. O'BRIEN,

IN THE
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ON APPEAL FROM THE UNITED STATES DISTRICT
COURT FOR THE WESTERN DISTRICT OF
WASHINGTON, SOUTHERN DIVISION

APPELLANT'S REPLY BRIEF

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IN THE
UNITED STATES
CIRCUIT COURT OF APPEALS
FOR THE NINTH CIRCUIT

WESTERN UNION TELEGRAPH COMPANY,
a corporation,

Appellant,

vs.

HANSEN & ROWLAND CORPORATION, a
corporation,

Appellee.

No. 11689

ON APPEAL FROM THE UNITED STATES DISTRICT
COURT FOR THE WESTERN DISTRICT OF
WASHINGTON, SOUTHERN DIVISION

APPELLANT'S REPLY BRIEF

The plaintiff's restatement of the case (Brief of Appellee, pp. 1-7) seems to have added for the consideration of this court no material fact not listed by the defendant's factual outline (Brief of Appellant, pp. 2-4; 7-9). The only aim of the plaintiff's restatement of the case appears to have been to justify the sum of \$750 per month as the reasonable rental value of the premises by recitals regarding the several extensions to the term of the old lease between the plaintiff and the defendant, which had fixed the rental at \$325 per month — an unnecessary effort, since the claim of the defendant's answer that \$500 per month was actually the maximum reasonable rental value, had been waived probably by the defendant's tenders

of \$750 per month and certainly by its stipulation of that amount as the reasonable rental value (R. 34, 39).

On the record in this case three possible rulings were open to the District Court, to-wit:

(a) TENANT BY AGREEMENT. That the defendant having impliedly accepted, by continued occupancy, the plaintiff's offer in its letter dated October 8th, the defendant's possession after October 31st was lawful, with the accompanying obligation to pay rent at \$1500 per month; and that, being in default as to fifty per cent of the agreed rent, the defendant was liable for the unpaid balance of rent, plus penalty in a sum equivalent to the whole rent (a total of \$3000 per month) under sub-section (3), §812, Rem. Rev. Stat.

(b) TRESPASSER. That the defendant having rejected the plaintiff's offer in its letter dated October 8th, the defendant's possession after October 31st was unlawful, with obligation to pay damages in the reasonable rental value of the premises at \$750 per month; and that, being a trespasser, the defendant was liable not only for damages in such amount, but also for penalty in a sum equivalent thereto (a total of \$1500 per month) under sub-section (1) of §812, Rem. Rev. Stat.

(c) TENANT BY SUFFERANCE. That the plaintiff, on November 2nd, by its alternative notice to quit the premises held or to pay the rental demanded (R. 45; Ex. 5), elected as a matter of Washington law to treat the defendant not as a trespasser but as a tenant whose possession was obtaining without the

plaintiff's consent in the absence of agreement as to the rate of rental, and whose obligation was limited to the payment of the reasonable rental value of the premises (at the rate of \$750 per month)—an obligation under Rem. Rev. Stat. §10621 already satisfied by the defendant's tenders to the plaintiff and payments into court.

The plaintiff's contention at the trial that the defendant was a *tenant by agreement* based on implied acceptance of the plaintiff's demand for payment of rental at \$1,500.00 per month resulting solely from the defendant's continued occupancy after October 31st, was rejected by the District Court (R. 7, 60, 62; Brief of Appellee, p. 14). In the face of the defendant's refusal to sign its acceptance of the plaintiff's proposal by letter of October 8th and in the face of the defendant's successive tenders of rental at \$750.00 per month, the plaintiff's contention was unsound (Ex. 3, 4, 6, 7, 8, 9; R. 44, 58, 59). The plaintiff's contention was advanced, before the lower court as before this court, without supporting citation of any Washington decision (Brief of Appellee, p. 14). The District Court rightly refused to adopt the plaintiff's theory that the defendant was a tenant by agreement with obligation to pay rental at \$1,500.00 per month and with liability for double penalty under sub-section (3) of §812. The plaintiff has not preserved its contention for reargument by cross-appeal (Brief of Appellee, p. 14).

With this simplification, the single problem remaining for determination in this case is whether

during its disputed occupancy beginning November 1st, 1946, and ending March 7th, 1947, the defendant was a *trespasser* under the penalty of sub-section (1) §812, or a *tenant by sufferance* under the protection of §10621.

The District Court held that the defendant was a trespasser, guilty of unlawful detainer as defined by sub-section (1) of §812, with liability to pay damages measured by the reasonable rental value of the premises at the rate of \$750 per month (tendered by defendant and deposited in court) and also with liability to pay penalty in the additional sum of \$750 per month.

This conclusion of the District Court, with its consequent judgment, the defendant contends was erroneous because on the particular facts involved the defendant was not guilty of unlawful detainer nor subject to the attached penalty, but rather was a tenant by sufferance without any default in payment of "reasonable rent" at the rate of \$750, which was its full legal liability under §10621.

In urging this contention the defendant is not disputing but applying the pertinent statutes of the State of Washington and the related opinions of the Washington Supreme Court. To maintain this contention the defendant need not quarrel with the authorities upon which the plaintiff relies by reference and quotation (Brief of Appellee, pp. 16-21). The plaintiff's cited cases merely declare that if an occupant is guilty of unlawful detainer under sub-section (1) of §812 it is liable to pay damages measured by the reasonable

rental value of the premises plus penalty in an additional equivalent amount.

The weakness of the District Court's ruling and of the plaintiff's position is that neither is supported by any Washington decision which adjudges upon a parallel chain of factual incidents that the occupant of premises was actually guilty of unlawful detainer—that being the only basis for liability to pay either damages as such or penalty thereon.

Again reciting for clarity and emphasis the particular facts of this case, during a period of years ending October 31, 1946, the defendant had been a tenant in lawful possession of the premises by valid written lease (with successive extensions each for a specified term) under which all rent was timely and fully paid (R. 37, 38, 57). After October 31st the defendant continued to occupy the premises until March 7th, 1947 (R. 40, 59).

On these facts the District Court was correct in concluding that if the defendant was at all guilty of unlawful detainer as variously prescribed by the several sub-sections of the Washington statute, it must be guilty only under the definition of sub-section (1) §812. To re-quote that provision, it reads:

“A tenant of real property * * * is guilty of unlawful detainer * * * when he holds over or continues in possession * * * after the expiration of the term for which it is let to him.

“In all cases where real property is leased for a specified term or period * * * the tenancy shall be terminated without notice at the expira-

tion of such specified term or period." (Sub-section (1) §812).

Because of the automatic extension clause contained in the formal written lease, the plaintiff's notice to stop the same by letter of July 24th was necessary (R. 40; Ex. 1). But the plaintiff and the defendant agree that as of October 31st, 1946, the lease was ended (Brief of Appellee, p. 3). Also they agree that the plaintiff's unqualified notice to surrender the premises, dated September 25th, was superfluous (Ex. 2; R. 42; Brief of Appellee, p. 3). Such notice was superfluous because of the latter portion of sub-section (1) §812, just quoted, and because of the language in §10620, Rem. Rev. Stat. (Brief of Appellee, p. 9).

The lease being terminated on October 31st, had the plaintiff allowed time alone to follow, the defendant would have been a trespasser guilty of unlawful detainer for "holding over" under sub-section (1), §812. However, the plaintiff had previously disclosed by its letter of October 8th (Ex. 3; R. 43) that, provided the defendant would pay \$1,500 per month to cover both reasonable rent and special damages as claimed, then the plaintiff was willing the defendant continue its occupancy. So, with its desire on the \$1,500 the plaintiff added another link to the chain of incidents by serving a third notice upon the defendant—the notice dated November 2, 1946, the alternative notice allowing the defendant the option either "to pay" or "to quit" (Ex. 5; R. 45).

This notice recited that the rental "became due and

payable on the first day of November, 1946;" it was retroactive.

This notice was not essential to perfect the plaintiff's right or remedy against the defendant as a trespasser for "holding over" under sub-section (1), §812, by which no notice whatsoever was required for any purpose.

This last notice by the plaintiff was purely voluntary.

Such a notice has been construed by the Washington Supreme Court to constitute an election by a landlord to treat an occupant of premises as a tenant rather than as a trespasser. In this ruling that court said:

"* * * although appellant entered without the knowledge or express permission of respondents, yet they immediately gave their permission by demanding the rent; and the notice to quit or pay rent, in itself shows permission on their part."

Williamson v. Hallett, 108 Wash. 176, 179,
182 Pac. 940, 941.

In other words, on November 2nd the plaintiff, by its own choice, elected to convert the defendant's unlawful possession into lawful possession on and after November 1st. However, the plaintiff's alternative notice of November 2nd could not alone effect agreement between the plaintiff and the defendant as to the rate of rental. Hence, by such notice, the defendant became not a tenant by contract but a tenant by law, since the defendant's possession obtained without permission or consent of the plaintiff in the

absence of rental payment as demanded at the rate of \$1,500 per month.

Such tenancy by operation of law, known as tenancy by sufferance in the State of Washington, is declared by statute in Rem. Rev. Stat. §10621 and recognized by decision in numerous cases, of which the defendant has already cited a few:

Klee v. U. S., 53 F.(2d) 58, 59, 61 (C.C.A. 9);

McCourtie v. Bayton, 159 Wash. 418, 422, 423, 294 Pac. 238, 240;

Provident Mutual Life Insurance Co. v. Thrower, 155 Wash. 613, 616; 285 Pac. 654, 655;

Williamson v. Hallett, 108 Wash. 176, 178, 179; 182 Pac. 940, 941.

Struggling against the obvious conclusion, from which the defendant would be exonerated of all liability to the plaintiff over and above the reasonable rental value of the premises at the rate of \$750, which had been timely and fully tendered month by month, the plaintiff argues that "to constitute a tenancy by sufferance" a necessary condition is the "obtaining possession of the premises without the consent of the owner"—a "condition not present here" because the defendant "was let into peaceful possession of the premises by the owner under a valid lease" (Brief of Appellee, pp. 9, 10).

But the plaintiff's argument assumes incorrect and unfair limitation of the meaning of the word "obtains" in the text of Rem. Rev. Stat. §10621. The

verb is defined to mean not only "to gain," "to procure," "to acquire," but also "to hold," "to keep," "to possess," "to occupy" and "to have a firm footing," "to be recognized or established," and "to be prevalent or general, as the custom *obtains*" (Webster's New International Dictionary [2nd Ed.] p. 1682).

Further the plaintiff's argument is incompatible with the established law of Washington as reflected by the State Supreme Court through its most recent applicable decision in *Davis v. Jones*, 15 Wn.(2d) 572; 131 P.(2d) 430.

In that case the defendant occupant, according to the court's recitals (Opinion: 131 P.(2d) 432) had "refused to pay the rent" in any amount before suit. On that account the defendant there was held guilty of unlawful detainer under sub-section (3), §812, and held liable for penalty despite delayed tenders into court after suit—for which latter reason the holding was cited by the plaintiff in the present case (Brief of Appellee, p. 19).

However, in citing that case the plaintiff missed or disregarded the facts disclosed in the court's opinion surrounding and initiating the tenancy of the defendant occupant, which was judicially classified as a tenancy by sufferance.

In that case certain residence property was owned by a sister and managed by her brother who, during his lifetime, permitted the defendant occupant to use the same without obligation for or payment of rent. After the brother's death the sister as owner of the premises demanded rent, which was totally

refused by the defendant occupant on the claim that no relationship of landlord and tenant existed.

The court ruled that the sister as owner was bound by her brother's act as the manager of the premises in allowing the defendant occupant to use the same rent free until the brother's death; but that *thereafter the continued occupancy of the defendant "constituted a tenancy by sufferance,"* (Opinion: 131 P.(2d) 431) under which the defendant had been bound to pay the reasonable rental value of the property as provided by §10621.

This "last word" of the Washington Supreme Court in *Davis v. Jones*, 15 Wn.(2d) 572; 131 P.(2d) 430, demonstrates that a tenancy by sufferance can follow an original possession which is both peaceful and lawful; and rejects clearly and completely the plaintiff's argument in the present case that tenancy by sufferance cannot arise except from an initial unlawful entry.

Next the plaintiff argues that tenancy by sufferance could exist only in the "absence of a demand on the part of the owner for a surrender of possession," and that "the statutory written demand was made on" the defendant in this case by the plaintiff (Brief of Appellee, pp. 9, 10).

This argument, while sound as a matter of law is unsound as a matter of fact on the record in this case, since the last and final demand served upon the defendant by the plaintiff was its notice of November 2nd (Ex. 5; R. 45), alternatively allowing the defendant "to pay" or "to quit"—the very same notice

from which the tenancy by sufferance arose, according to the law of Washington as declared by its Supreme Court, in the light of which it would be illogical and inconsistent to rule that this identical notice in a single moment should operate both to create and destroy such a tenancy.

After the service of this notice on November 2nd during the defendant's continued occupancy, the plaintiff never made any unqualified or absolute demand for surrender of the premises. Even in this action the plaintiff refrained from praying in its complaint or seeking by other application the issuance of a writ of restitution for immediate restoration of possession as authorized by §819 Rem. Rev. Stat. (R. 7, 8).

The simple, unadulterated truth is the plaintiff wanted the \$750 per month, being paid, if the plaintiff couldn't get the \$1,500 per month, being demanded.

Concluding its argument plaintiff asserts that this appeal "is so devoid of merit" as to "present the appearance of having been sued out merely for delay" and as to warrant imposition of punitive damages under this court's Rule 26 (Brief of Appellee, pp. 24, 25).

Concluding its reply argument in the same spirit of charity, the defendant suggests that the plaintiff's demand of \$1,500 per month (to cover \$750 as "reasonable rental," which admittedly was duly tendered, and to cover \$750 special damages, which admittedly were never suffered) was so extortionate as

to place the defendant in a position of equity, entitling it to every legal and just relief within the power of this court.

Respectfully submitted,

LANE SUMMERS,

Attorney for Appellant.

F. T. MERRITT,

G. H. BUCEY,

Of Counsel.

No. 11690

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

PASADENA RESEARCH LABORATORIES, INC.,
a corporation, and RUSSELL R. BAVOUCSET,
Appellants,

vs.

UNITED STATES OF AMERICA,
Appellee.

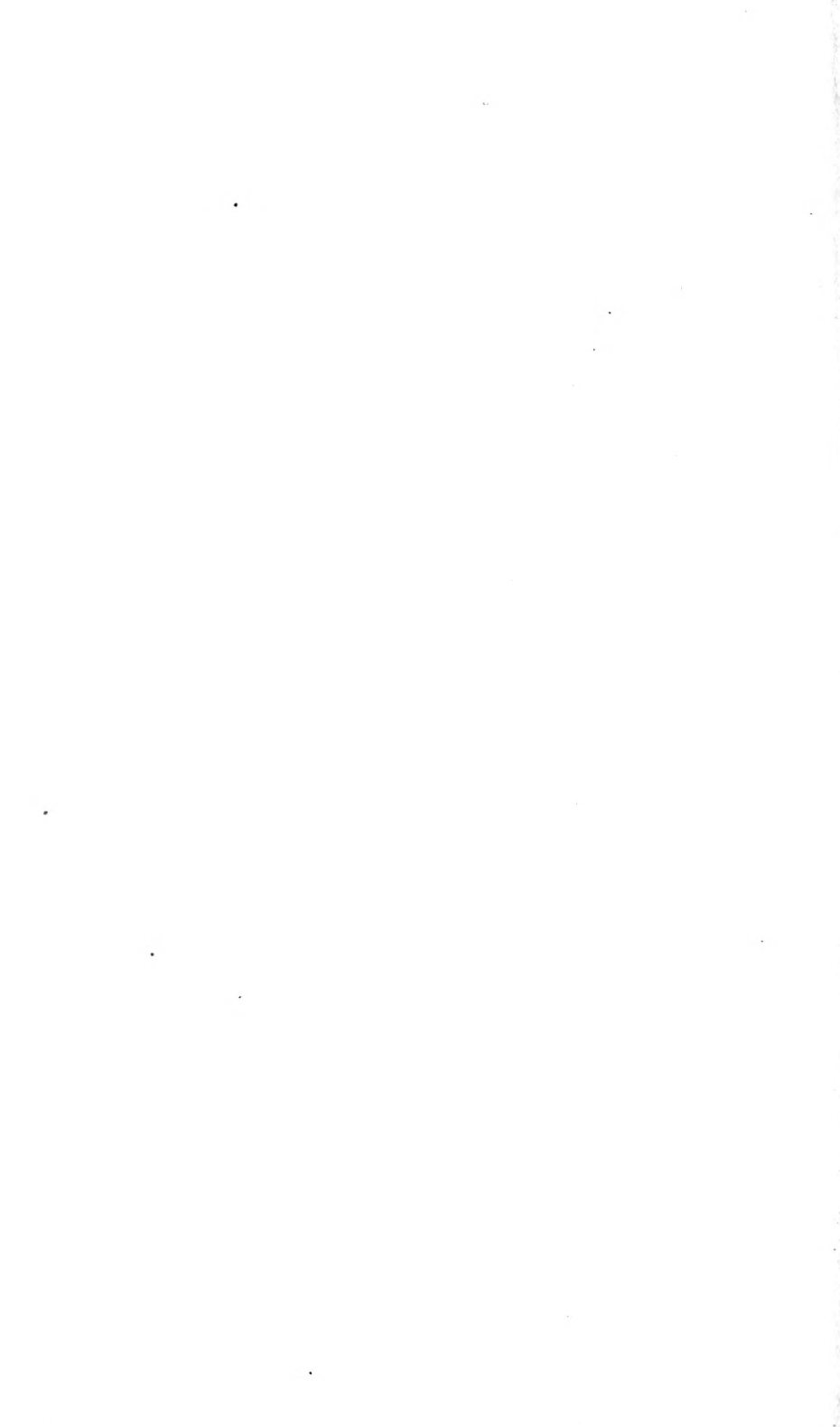
TRANSCRIPT OF RECORD

Upon Appeals from the District Court of the United States
for the Southern District of California,
Central Division

FILED

NOV 14 1947

PAUL P. O'BRIEN,
CLERK



No. 11690

IN THE

United States Circuit Court of Appeals
FOR THE NINTH CIRCUIT

PASADENA RESEARCH LABORATORIES, INC.,
a corporation, and RUSSELL R. BAVOuset,
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Upon Appeals from the District Court of the United States
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F. D. C. No. 21441

In the District Court of the United States for the
Southern District of California
Central Division

No. 19223

UNITED STATES OF AMERICA

v.

PASADENA RESEARCH LABORATORIES, INC.,
a corporation, and RUSSELL R. BAVOuset, an
individual.

INFORMATION
(21 U. S. C. 331 and 333)

COUNT I

[21 U. S. C. 331(a), 333(a), 351(c)]

The United States Attorney charges:

That the Pasadena Research Laboratories, Inc., a corporation organized and existing under the laws of the State of California and trading and doing business at Pasadena, State of California, and Russell R. Bavouset, an individual, at the time hereinafter mentioned Secretary-Treasurer of said corporation, did, within the Southern District of California, on or about September 17, 1945, in violation of the Federal Food, Drug, and Cosmetic Act, unlawfully cause to be introduced and delivered for introduction into interstate commerce, at Pasadena, State of California, for delivery to Cheyenne, State of Wyoming, consigned to Dr. Joseph C. Bunten, a number of vials containing a drug;

That displayed upon said vials, when caused to be introduced and delivered for introduction into interstate

commerce as aforesaid, was the following printed and graphic matter:

30 cc Vial	STERILE	No. 92
	INDOFORM	

EACH CC CONTAINS:

Suprarenal Cortex	30 grs.	Whole Ovarian	40 grs.
Anterior Pituitary	30 grs.	Thymus Substance	15 grs.
Posterior Pituitary		Thyroid Substance	1 gr.
	3 Int'l Units	Lymphatic Substance	5 grs.

Preserved with Chlorobutanol (Chloroform Derivative)
0.5% (w/v) and Tricresol 0.5% (v/v)

This preparation does not contain any known
therapeutically useful constituent.

Caution: To be used only by or on the
prescription of a physician. [2]

PASADENA RESEARCH LABORATORIES, Inc.
Pasadena 8, Calif., U. S. A.

Lot No. 728

That said drug, when caused to be introduced and delivered for introduction into interstate commerce as aforesaid, was then and there adulterated within the meaning of 21 U. S. C. 351(c), in that its strength differed from that which it purported and was represented to possess, in that each cubic centimeter of said drug purported and was represented to contain 3 International Units of Posterior Pituitary and 1 grain of Thyroid Substance, whereas, in fact and in truth, each cubic centimeter of said drug did not contain 3 International Units of Posterior Pituitary but did contain less than that amount of Posterior

Pituitary, and each cubic centimeter of said drug did not contain 1 grain of Thyroid Substance but did contain no Thyroid Substance.

COUNT II

[21 U. S. C. 331, 333, 352(a)]

The United States Attorney further charges:

That the Pasadena Research Laboratories, Inc., a corporation organized and existing under the laws of the State of California and trading and doing business at Pasadena, State of California, and Russell R. Bavouset, an individual, at the time hereinafter mentioned Secretary-Treasurer of said corporation, did, within the Southern District of California, on or about September 17, 1945, in violation of the Federal Food, Drug, and Cosmetic Act, unlawfully cause to be introduced and delivered for introduction into interstate commerce, at Pasadena, State of California, for delivery to Cheyenne, State of Wyoming, consigned to Dr. Joseph C. Bunten, a number of vials containing a drug;

That displayed upon said vials, when caused to be introduced and delivered for introduction into interstate commerce as aforesaid, was the printed and graphic matter displayed upon the vials described in the first count of this information, which said description in said first count, is, by reference, hereby incorporated in this count; [3]

That said drug, when caused to be introduced and delivered for introduction into interstate commerce as aforesaid, was then and there misbranded within the meaning of 21 U. S. C. 352(a), in that the statements, to wit, "Each CC Contains: * * * Posterior Pituitary 3 Int'l Units * * * Thyroid Substance 1 gr.", displayed on the

vials containing said drug as aforesaid, were false and misleading in this, that the said statements represented and suggested that each cubic centimeter of said drug contained 3 International Units of Posterior Pituitary and 1 grain of Thyroid Substance whereas, in fact and in truth, each cubic centimeter of said drug did not contain 3 International Units of Posterior Pituitary, but did contain less than that amount of Posterior Pituitary, and each cubic centimeter of said drug did not contain 1 grain of Thyroid Substance but did contain no Thyroid Substance.

COUNT III

[21 U. S. C. 331, 333, 351(c)]

The United States Attorney further charges:

That the Pasadena Research Laboratories, Inc., a corporation organized and existing under the laws of the State of California and trading and doing business at Pasadena, State of California, and Russell R. Bavouset, an individual, at the time hereinafter mentioned Secretary-Treasurer of said corporation, did, within the Southern District of California, on or about July 16, 1945, in violation of the Federal Food, Drug, and Cosmetic Act, unlawfully cause to be introduced and delivered for introduction into interstate commerce, at Pasadena, State of California, for delivery to Reno, State of Nevada, consigned to Dr. Clement Swaim, a number of vials containing a drug;

That displayed upon said vials, when caused to be introduced and delivered for introduction into interstate commerce as aforesaid, was the following printed and graphic matter:

30 CC	STERILE SOLUTION	No.256
	PLURI-B	[4]

(Some factors of the B Complex)
For Intramuscular Use

EACH CC CONTAINS:

Thiamine Hydrochloride	50 Mgms.
Riboflavin	1 Mgm.
Pyridoxine Hydrochloride	10 Mgms.
Pantothenic Acid	10 Mgms.
Nicotinamide	50 Mgms.
Chlorobutanol (Chloroform deriv.)	1/12 gr.—0.005 gm.

CAUTION: To be used only by or on the
prescription of a physician.

PASADENA RESEARCH LABORATORIES, Inc.
Pasadena 8, Calif., U. S. A.

That said drug, when caused to be introduced and delivered for introduction into interstate commerce as aforesaid, was then and there adulterated within the meaning of 21 U. S. C. 351(c), in that its strength differed from that which it purported and was represented to possess, in that said drug purported and was represented to contain 50 milligrams of thiamine hydrochloride in each cubic centimeter, whereas, in fact and in truth, said drug did not contain 50 milligrams of thiamine hydrochloride in each cubic centimeter, but did contain less than that amount of thiamine hydrochloride.

COUNT IV

[21 U. S. C. 331, 333, 352(a)]

The United States Attorney further charges:

That the Pasadena Research Laboratories, Inc., a corporation organized and existing under the laws of the State of California and trading and doing business at Pasadena, State of California, and Russell R. Bavouset, an individual, at the time hereinafter mentioned Secretary-Treasurer of said corporation, did, within the Southern District of California, on or about July 16, 1945, in violation of the Federal Food, Drug, and Cosmetic Act, unlawfully cause to be introduced and delivered for introduction into interstate commerce, at Pasadena, State of California, for delivery to Reno, State of Nevada, consigned to Dr. Clement Swain, a number of vials containing a drug; [5]

That displayed upon said vials, when caused to be introduced and delivered for introduction into interstate commerce as aforesaid, was the printed and graphic matter displayed upon the vials described in the third count of this information, which said description in said third count, is, by reference, hereby incorporated in this count;

That said drug, when caused to be introduced and delivered for introduction into interstate commerce as aforesaid, was then and there misbranded within the meaning of 21 U. S. C. 352(a), in that the statement, to wit, "Each CC Contains * * * Thiamine Hydrochloride—50 Mgms.", displayed on the vials containing said drug as

aforesaid, was false and misleading in this, that the said statement represented and suggested that said drug contained 50 milligrams of Thiamine Hydrochloride in each cubic centimeter whereas, in fact and in truth, said drug did not contain 50 milligrams of Thiamine Hydrochloride in each cubic centimeter, but did contain less than that amount of Thiamine Hydrochloride.

COUNT V

[21 U. S. C. 331, 333, 351(a)]

The United States Attorney further charges:

That the Pasadena Research Laboratories, Inc., a corporation organized and existing under the laws of the State of California and trading and doing business at Pasadena, State of California, and Russell R. Bavouset, an individual, at the time hereinafter mentioned Secretary-Treasurer of said corporation, did, within the Southern District of California, on or about November 19, 1945, in violation of the Federal Food, Drug, and Cosmetic Act, unlawfully cause to be introduced and delivered for introduction into interstate commerce, at Pasadena, State of California, for delivery to Sunnyside, State of Washington, consigned to Dr. C. A. Hughes, one vial containing a drug;

That displayed upon said vial, when caused to be introduced and delivered for introduction into interstate commerce as aforesaid, was the following printed and graphic matter: [6]

15 CC STERILE No. 270
 INJECTABLE
 VITAMIN D (In Oil)
 (Activated Ergosterol)
 For Intramuscular Use
500,000 U. S. P. Units Per cc.

CAUTION: To be used only by or on the
prescription of a physician.

PASADENA RESEARCH LABORATORIES
Pasadena 8, Calif., U. S. A.

That said drug, when caused to be introduced and delivered for introduction into interstate commerce as aforesaid, was then and there adulterated within the meaning of 21 U. S. C. 351(c), in that its strength differed from that which it purported and was represented to possess, in that said drug purported and was represented to contain 500,000 U. S. P. Units of Vitamin D per cubic centimeter, whereas, in fact and in truth, said drug did not contain 500,000 U. S. P. Units of Vitamin D per cubic centimeter but did contain less than that amount of Vitamin D.

COUNT VI

[21 U. S. C. 331, 333, 352(a)]

The United States Attorney further charges:

That the Pasadena Research Laboratories, Inc., a corporation organized and existing under the laws of the State of California and trading and doing business at Pasadena, State of California, and Russell R. Bavouset, an individual, at the time hereinafter mentioned Secretary-Treasurer of said corporation, did, within the Southern District of California, on or about November 19,

1945, in violation of the Federal Food, Drug, and Cosmetic Act, unlawfully cause to be introduced and delivered for introduction into interstate commerce, at Pasadena, State of California, for delivery to Sunnyside, State of Washington, consigned to Dr. C. A. Hughes, one vial containing a drug;

That displayed upon said vial, when caused to be introduced and delivered for introduction into interstate commerce as aforesaid, was [7] the printed and graphic matter displayed upon the vial described in the fifth count of this information, which said description in said fifth count, is, by reference, hereby incorporated in this count;

That said drug, when caused to be introduced and delivered for introduction into interstate commerce as aforesaid, was then and there misbranded within the meaning of 21 U. S. C. 352(a), in that the statement, to wit, "Vitamin D * * * 500,000 U. S. P. Units per cc.", displayed on the vial containing said drug as aforesaid, was false and misleading in this, that the said statement represented and suggested that said drug contained 500,000 U. S. P. Units of Vitamin D per cubic centimeter whereas, in fact and in truth, said drug did not contain 500,000 U. S. P. Units of Vitamin D per cubic centimeter, but did contain less than that amount of Vitamin D.

COUNT VII

[21 U. S. C. 331, 333, 351(c)]

The United States Attorney further charges:

That the Pasadena Research Laboratories, Inc., a corporation organized and existing under the laws of the State of California and trading and doing business at Pasadena, State of California, and Russell R. Bavouset, an individual, at the time hereinafter mentioned Secre-

tary-Treasurer of said corporation, did, within the Southern District of California, on or about June 18, 1946, in violation of the Federal Food, Drug, and Cosmetic Act, unlawfully cause to be introduced and delivered for introduction into interstate commerce, at Pasadena, State of California, for delivery to Phoenix, State of Arizona, consigned to Dr. P. M. Ryerson, a number of vials containing a drug;

That displayed upon said vials, when caused to be introduced and delivered for introduction into interstate commerce as aforesaid, was the following printed and graphic matter:

30 cc	STERILE SOLUTION	No. 256
	PLURI-B	[8]

(Some factors of the B Complex)

For Intramuscular or Intravenous Use

EACH CC CONTAINS:

Thiamine Hydrochloride	50 Mgms.
Riboflavin	2 Mgms.
Pyridoxine Hydrochloride	10 Mgms.
Pantothenic Acid	10 Mgms.
Nicotinamide	50 Mgms.
Chlorobutanol (Chloroform deriv.)	1/12 gr.—0.005 gm.

Caution: To be dispensed only by or on the
Prescription of a physician.

Lot No. 317

PASADENA RESEARCH LABORATORIES, Inc.

Pasadena 8, Calif., U. S. A.

That said drug, when caused to be introduced and delivered for introduction into interstate commerce as aforesaid, was then and there adulterated within the meaning

of 21 U. S. C. 351(c), in that its purity and quality fell below that which it purported and was represented to possess, in that said drug purported and was represented to be a drug suitable and appropriate for intramuscular and intravenous administration, to wit, injection into the muscular tissues and veins, a use which requires a product free from undissolved material, whereas said drug was unsuitable and inappropriate for intramuscular and intravenous administration in that said drug contained undissolved material.

JAMES M. CARTER

United States Attorney for the Southern
District of California

By Alfred P. Chamie
Assistant United States Attorney

[Endorsed]: Filed Mar. 18, 1947. [9]

[Minutes: Monday, April 7, 1947]

Present: The Honorable Wm. C. Mathes, District Judge.

This cause coming on for plea of defendants Pasadena Research Laboratories, Inc., a corporation, and Russell R. Bavouset; R. H. Kinnison, Assistant U. S. Attorney, appearing as counsel for the Government; John C. Stick, Esq., appearing as counsel for the defendants; Russell R. Bavouset, defendant, being present on his own recognizance, and as secretary and treasurer of the defendant corporation; defendant Russell R. Bavouset in his own behalf and that of the defendant corporation pleads not guilty to all counts of the Information.

It is ordered that the cause is hereby set for trial on June 17, 1947, at 10 A. M., before Judge Weinberger. [10]

[Title of District Court and Cause]

STIPULATION PERTAINING TO INTERSTATE
SHIPMENT AND CERTAIN FACTS RELE-
VANT THERETO

It Is Hereby Stipulated by and between James M. Carter, United States Attorney, and Norman W. Neukom, Assistant United States Attorney, for and on behalf of the plaintiff, and John C. Stick, attorney for the defendants, as follows:

I.

That at the time of the trial of the herein action the Government need not offer any proof as to the interstate shipment of the drug or products set forth in each and every count of the herein Information; it being stipulated that the named defendants did ship or did cause to be shipped in interstate commerce, on or about the dates set forth in each of the respective counts of the Information, the drug or product herein named and described, from Los Angeles, California, to the named consignees at the location or place designated in each of the respective counts of said Information. [11]

II.

It Is Further Stipulated that there was displayed upon the vials or containers of the product or drug described in each of the counts of said Information, when caused to be so introduced and delivered in interstate commerce, labels stating substantially the printed and graphic matter as is alleged in each of the counts of said Information, either in words and figures or by reference to another count.

III.

It Is Further Stipulated that each of the designated and named consignees did receive, shortly after the date of each shipment, one or more vials or packages containing the product or drug so shipped in interstate commerce by the named defendants.

IV.

So as to shorten the time of trial and to avoid the necessity of any unnecessary testimony, It Is Further Stipulated with respect to each of the counts that the additional following factual matter is stipulated to; it being understood and agreed that if the persons named were called to the stand he would testify under oath to the following facts:

V.

(With reference to Counts One and Two)

The described product "Indoform" was shipped by the defendants on or about September 17, 1945, in interstate commerce, from Pasadena, California, to Dr. Joseph C. Bunten, Cheyenne, Wyoming, said shipment consisting of a number of vials containing a product or drug bearing, at time of said shipment, labels stating substantially the printed and graphic matter as is set out in Counts One and Two. That on or about January 24, 1946, a sample consisting of one vial and contents from said shipment was collected by Inspector Ralph M. Davidson, Federal Food and Drug Inspector, from the said Dr. Joseph C. Bunten; that the said Inspector marked and identified the label on the vial "27131 H, 1/24/46 RMD"; that he sealed the vial and contents with an official seal identified "27131 H, 1/24/46 Ralph M.

Davidson"; that the sample and contents so identified and [12] sealed was forwarded by the Inspector by U. S. Mail to Pharmacology Division, Food and Drug Administration, Washington, D. C.

VI.

(With reference to Counts Three and Four)

The described product "Pluri-B" was shipped by the defendants on or about July 16, 1945, in interstate commerce, from Pasadena, California, to Dr. Clement Swaim, 125 North Virginia, Reno, Nevada, consisting of a number of vials containing a product or drug bearing at said time on the container substantially the printed and graphic matter as is set out in Counts Three and Four. That on or about August 30, 1945, a sample consisting of two vials and contents from said shipment was obtained by Inspector Frank A. Griebeling of Federal Food and Drug Administration, from the said Dr. Clement Swaim; that the said Inspector sealed the vials and contents with official seals marked and identified "29953 H, 8/30/45 Frank A. Griebeling"; that the sample and contents so identified and sealed was forwarded by the Inspector, by U. S. Mail, to Vitamin Division, Food and Drug Administration, Washington, D. C.

VII.

(With reference to Counts Five and Six)

The described product "Vitamin D" was shipped by the defendants on or about November 25, 1945, in interstate commerce, from Pasadena, California, to Dr. C. A. Hughes, Sunnyside, Washington, namely, a vial containing a product or drug and bearing the label substantially

as is set out in Counts Five and Six. That on or about January 9, 1946, this vial and contents was obtained as a sample by Inspector Charles C. Cooley of Federal Food and Drug Administration, from the said Dr. C. A. Hughes; that the said Inspector identified and marked the label on the vial "58019 H, 1/9/46 CCC"; that he sealed the carton holding the vial and contents with an official seal identified "58019 H, 1/9/46 Charles C. Cooley"; that the sample and contents so identified and sealed was forwarded by the Inspector, by U. S. Mail, to Pharmacology Division, Food and Drug Administration, Washington, D. C. [13]

VIII.

(With reference to Count Seven)

The described product "Pluri-B" was shipped by the defendants on or about June 18, 1946, in interstate commerce, from Pasadena, California, to Dr. P. M. Ryerson, 1505 E. McDowell Road, Phoenix, Arizona, consisting of a number of vials containing a product or drug bearing at said time a label stating substantially the printed and graphic matter as is set out in Count Seven. That on or about July 12, 1946, Inspector Maurice P. Kerr, Federal Food and Drug Inspector, collected a sample consisting of six vials and contents, each at random from different boxes of the said shipment in the possession of Dr. P. M. Ryerson; that the said Inspector marked and identified the labels on the vials "30694 H, 7/12/46 MPK"; that he sealed the vials and contents with official seals identified "30694 H, 7/12/46 Maurice P. Kerr"; that the samples and contents so identified and sealed were forwarded by the Inspector by Railway Express to

Pharmacology Division, Food and Drug Administration,
Washington, D. C.

Dated this 10 day of June, 1947.

JAMES M. CARTER

United States Attorney

NORMAN W. NEUKOM

Assistant U. S. Attorney

Chief of Criminal Division

Attorneys for Plaintiff

JOHN C. STICK

Attorney for Defendants

[Endorsed]: Filed Jun. 17, 1947. [14]

[Title of District Court and Cause]

WAIVER OF TRIAL BY JURY AND WAIVER
OF SPECIAL FINDINGS OF FACT
(Rule 23(a) and (c) F. R. C. P.)

The undersigned defendant hereby waives the right to a trial by jury and requests the court to try all charges against him in this cause without a jury.

The undersigned defendant further waives the right to request any special findings of fact as provided by Rule 23(c) of the Federal Rules of Criminal Procedure.

June 17, 1947.

PASADENA RESEARCH LABS., INC.

By Russell R. Bavouset

Gen. Mgr.

RUSSELL R. BAVOuset

Defendant

The undersigned counsellor represents that prior to the signing of the foregoing waiver, the defendant was fully advised as to the rights of an accused under the Constitution and laws of the United States, including the right to a trial by jury and the right to request special findings in a case tried without a jury; and further represents that, in his opinion, the above waiver by the defendant of trial by jury and special findings is voluntarily and understandingly made.

June 17, 1947.

JOHN C. STICK

Attorney for Defendants

The United States Attorney hereby consent that the case be tried without a jury, and waives the right to request any special findings of fact as provided by Rule 23(c) of the Federal Rules of Criminal Procedure.

June 17, 1947.

JAMES M. CARTER

United States Attorney

By Norman W. Neukom

Assistant U. S. Attorney

Approved June 17, 1947.

WM. C. MATHES

United States District Judge

[Endorsed]: Filed Jun. 17, 1947. [15]

[Minutes: Friday, June 20, 1947]

Present: The Honorable Wm. C. Mathes, District Judge.

Further trial;

Norman Neukom, Asst. U. S. Atty., appearing for the Government;

John C. Stick, Esq., appearing for the defendants;

Defendant's Exhibits A, B, C, D, and E for identification are marked in evidence at Atty. Stick's request. Witness Jike resumes his testimony. The defense rests.

Witness Tolle, heretofore sworn, testifies further. Witness Mason, heretofore sworn, testifies further. Witness Wiley, heretofore sworn, resumes his testimony. The Government rests.

At 11:52 A. M. Attorney Neukom argues for the plaintiff. At 12:20 P. M. Court recesses.

At 1:52 P. M. Court reconvenes, all being present as before, at 2:02 P. M. Attorney Stick argues for defendants. At 2:45 P. M. Attorney Neukom argues for U. S. in rebuttal.

The Court finds both defendants guilty on counts 1, 2, 3 and 7 and not guilty on counts 5 and 6 and the cause is ordered referred to the Probation Officer for report and is continued to July 7, 1947, 1:30 P. M. for sentence.

Pursuant to stipulation, it is ordered that exhibits may be returned to parties at expiration of appeal period if no appeal is taken. [16]

District Court of the United States for the
Southern District of California
Central Division

No. 19223

Criminal Information in Seven Counts for Violation of
21 U. S. C. 331(a), 333(a), 351(c)

UNITED STATES OF AMERICA

v.

PASADENA RESEARCH LABORATORIES, INC.

JUDGMENT

On this 7th day of July, 1947 came the attorney for the government and the defendant appeared in person and with John C. Stick, Esquire, its counsel.

It Is Adjudged that the defendant has been convicted upon its plea of not guilty and finding of guilty by the court, after trial without a jury, jury trial having been waived, of the offenses of transporting in interstate commerce drugs, some of which were misbranded, and others were adulterated, in that their strength was not as indicated on the labels, as charged in Counts One, Two, Three, Four and Seven of the information; and the court having asked the defendant whether it has anything to say why judgment should not be pronounced, and no sufficient cause to the contrary being shown or appearing to the Court,

It Is Adjudged that the defendant is guilty as charged and convicted.

It Is Adjudged that the defendant pay to the United States of America a fine of \$1,000 for the offense charged in the First Count of the information; and a fine of \$1,000 for the offense charged in the Second Count of the information; and a fine of \$1,000 for the offense charged in the Third Count of the information; and a fine of \$1,000 for the offense charged in the Fourth Count of the information; and a fine of \$1,000 for the offense charged in the Seventh Count of the information.

It Is Further Adjudged that payment of a single fine of \$1,000 shall satisfy the fines imposed under Counts One and Two of the information; and that a single fine of \$1,000 shall satisfy the fines imposed under Counts Three and Four of the information; and that payment of a total fine of \$3,000 shall fully satisfy and discharge all fines imposed under Counts One, Two, Three, Four and Seven.

It is Adjudged that the defendant is not guilty of the offenses charged in Counts Five and Six of the information.

It Is Further Adjudged that execution of this judgment be stayed until 12 o'clock noon on July 14, 1947.

WM. C. MATHES

United States District Judge

[Endorsed]: Filed Jul. 7, 1947. [17]

District Court of the United States for the
Southern District of California
Central Division

No. 19223

Criminal Information in Seven Counts for Violation of
21 U. S. C. 331(a), 333(a), 351(c)

UNITED STATES OF AMERICA

v.

RUSSELL R. BAVOUSET

PROBATIONARY ORDER

On this 7th day of July, 1947 came the attorney for the government and the defendant appeared in person and with his counsel John C. Stick, Esquire.

It Is Adjudged that the defendant has been convicted upon his plea of not guilty and finding of guilty by the court, after trial without a jury, jury trial having been waived, of the offenses of transporting in interstate commerce drugs, some of which were misbranded, and others adulterated, in that their strength was not as indicated on the labels, as charged in Counts One, Two, Three, Four and Seven of the information; and the court having asked the defendant whether he has anything to say why judgment should not be pronounced, and no sufficient cause to the contrary being shown or appearing to the Court,

It Is Adjudged that the defendant is guilty as charged and convicted.

It Is Adjudged that imposition of sentence for the offenses charged in Counts One, Two, Three, Four and

Seven of the information be and is hereby suspended, and the defendant is placed on probation for the period of five years commencing forthwith; and the conditions of probation are fixed as follows: during the probationary period the defendant shall (1) donate \$5 or more each month from his personal earnings to a charity of his own choice, approved by the Probation Officer of this Court; (2) obey all laws applicable to his conduct; and (3) comply with all rules which the Probation Officer of this Court shall prescribe for the guidance of his personal conduct.

It Is Further adjudged that the probationary periods and the conditions of probation shall be the same as to the First, Second, Third, Fourth and Seventh Counts; that the probationary periods shall commence and run concurrently; that compliance with the conditions of probation as to the First Count shall also constitute compliance with the conditions of probation as to the Second, Third, Fourth and Seventh Counts; and that a violation of any of the conditions of probation as to the First Count shall likewise constitute a violation of the conditions as to the Second, Third, Fourth and Seventh Counts.

It Is Further Adjudged that the defendant is not guilty of the offenses charged in Counts Five and Six of the information.

WM. C. MATHES

United States District Judge

[Endorsed]: Filed Jul. 7, 1947. [18]

[Title of District Court and Cause]

NOTICE OF APPEAL BY DEFENDANT PASADENA RESEARCH LABORATORIES, INC., A CORPORATION

Name and address of appellant: Pasadena Research Laboratories, Inc., 2107 East Villa, Pasadena, California.

Name and address of appellant's attorneys: John C. Stick, 510 S. Spring Street, Los Angeles 13, California, and R. Welton Whann, 315 West Ninth Street, Los Angeles 15, California.

Offenses: Violation of the Federal Food, Drug and Cosmetic Act by misbranding and adulteration of drugs in violation of 21 U. S. C. 331(a), 351(c) and 352(a). [19]

Concise statement of judgment giving date and sentence: Defendant-appellant, Pasadena Research Laboratories, Inc., was found guilty on Counts 1, 2, 3, 4 and 7 of the information, and in the Judgment dated July 7, 1947, was sentenced to pay a fine of Three Thousand (\$3,000.00) Dollars, which fine of Three Thousand (\$3,000.00) Dollars has been paid.

Defendant-appellant Pasadena Research Laboratories, Inc., does hereby appeal to the United States Circuit Court of Appeals for the Ninth Circuit from the above-stated judgment.

Dated: July 16, 1947.

PASADENA RESEARCH LABORATORIES, INC.,
a corporation

By Russell R. Bavouset
Secretary-Treasurer
Defendant.

JOHN C. STICK

R. WELTON WHANN

Attorneys for Defendant-Appellant
Pasadena Research Laboratories, Inc.

Received copy of the above Notice of Appeal this 16 day of July, 1947. United States Attorney for the Southern District of California. By Norman W. Neukom, Asst. U. S. Attorney.

[Endorsed]: Filed Jul. 16, 1947. [20]

[Title of District Court and Cause]

NOTICE OF APPEAL BY DEFENDANT
RUSSELL R. BAVOuset, AN INDIVIDUAL

Name and address of appellant: Russell R. Bavouset, 2524 S. Sycamore, Los Angeles 16, California.

Name and address of appellant's attorneys: John C. Stick, 510 S. Spring Street, Los Angeles 13, California, and R. Welton Whann, 315 West Ninth Street, Los Angeles 15, California.

Offenses: Violation of the Federal Food, Drug and Cosmetic Act by misbranding and adulteration of drugs in violation of 21 U. S. C. 331(a), 351(c) and 352(a).

Concise statement of judgment giving date and sentence: Defendant-appellant Russell R. Bavouset was found guilty on [21] Counts 1, 2, 3, 4 and 7 of the information, and in the Judgment dated July 7, 1947, imposition of sentence was suspended and the defendant-appellant Russell R. Bavouset was placed on probation for a period of five (5) years under the conditions set forth in the probationary order dated July 7, 1947.

Defendant-appellant Russell R. Bavouset, does hereby appeal to the United States Circuit Court of Appeals for the Ninth Circuit from the above-stated judgment.

Dated: July 16, 1947.

RUSSELL R. BAVOuset
an individual
Defendant

JOHN C. STICK
R. WELTON WHANN

Attorneys for Defendant-Appellant
Russell R. Bavouset

Received copy of the above Notice of Appeal this 16 day of July, 1947. United States Attorney, Southern District of California. By Norman W. Neukom, Asst. U. S. Attorney.

[Endorsed]: Filed Jul. 16, 1947. [22]

[Title of District Court and Cause]

ASSOCIATION OF ATTORNEY

R. Welton Whann is hereby associated with John C. Stick as attorney for defendants in the above-entitled cause.

JOHN C. STICK

We, Pasadena Research Laboratories, Inc., and Russell R. Bavouset, the above-named defendants, do hereby consent to and approve of the above association of attorney.

PASADENA RESEARCH LABORATORIES, INC.,
a corporation

By Russell R. Bavouset

Secretary-Treasurer

RUSSELL R. BAVOuset

an individual [23]

I, R. Welton Whann, hereby accept the above association.

R. WELTON WHANN

Receipt of a copy of the above association of attorneys is hereby acknowledged this 16 day of July, 1947. United States Attorney for the Southern District of California.
By Norman W. Neukom, Asst.

[Endorsed]: Filed Jul. 16, 1947. [24]

[Title of District Court and Cause]

STIPULATION AND ORDER FOR TRANSMIS-
SION OF ORIGINAL PAPERS AND EXHIBITS

It Is Hereby Stipulated and Agreed, by and between the parties hereto that the Court may, if it approves, enter an order herein in the form provided for below.

Dated: Los Angeles, California, this 20 day of August, 1947.

JAMES M. CARTER

United States Attorney

RAY H. KINNISON

Assistant United States Attorney

Attorneys for Plaintiff

JOHN C. STICK

R. WELTON WHANN

By R. Welton Whann

Attorneys for Defendants [28]

It appearing that it is desirable that certain original papers and exhibits on file in the above cause should be inspected by the Circuit Court of Appeals for the Ninth Circuit, notice of appeal to that Court having been filed in this cause,

It Is Hereby Ordered, pursuant to Rule 75(i) of the Rules of Civil Procedure, that the Clerk of this Court forward, all costs thereof to be paid by Pasadena Research Laboratories, Inc. and Russell R. Bavouset, defendants-appellants, to the Clerk of the Circuit Court of Appeals for the Ninth Circuit, all original papers and other exhibits, said papers and exhibits to be held by the Clerk of the Appellate Court pending the appeal, and to be returned to the Clerk of this Court unless otherwise provided by the rules of said Appellate Court.

Dated at Los Angeles, California, this 20 day of August, 1947.

JACOB WEINBERGER

United States District Judge

[Endorsed]: Filed Aug. 20, 1947. [29]

[Title of District Court and Cause]

CERTIFICATE OF CLERK

I, Edmund L. Smith, Clerk of the District Court of the United States for the Southern District of California, do hereby certify that the foregoing pages numbered from 1 to 29, inclusive, contain full, true and correct copies of Information; Minute Order Entered April 7, 1947; Stipulation Pertaining to Interstate Shipment and Certain Facts Relevant Thereto; Waiver of Trial by Jury and of Special Findings of Fact; Minute Order Entered June 20, 1947; Judgment as to Defendant Pasadena Research Laboratories, Inc.; Probationary Order as to Defendant Russell R. Bavouset; Notice of Appeal as to each of the Defendants; Association of Attorney; Designation of Record on Appeal and Stipulation and Order for Transmission of Original Exhibits which, together with the Original Exhibits and copy of Reporter's Transcript, transmitted herewith, constitute the record on appeal to the United States Circuit Court of Appeals for the Ninth Circuit.

I further certify that my fees for preparing, comparing, correcting and certifying the foregoing record amount to \$8.20 which sum has been paid to me by appellants.

Witness my hand and the seal of said District Court this 20th day of August, 1947.

(Seal)

EDMUND L. SMITH

Clerk

By Theodore Hocke

Chief Deputy Clerk

[Title of District Court and Cause]

REPORTER'S TRANSCRIPT OF PROCEEDINGS

Los Angeles, California, Tuesday, June 17, 1947

Appearances:

For the Plaintiff: James M. Carter, Esq., United States Attorney; by Norman W. Neukom, Esq., Asst. U. S. Attorney.

For the Defendants: John C. Stick, Esq., and Eugene M. Ellison, Esq.

* * * * *

[Mr. Neukom made an opening statement on behalf of the plaintiff.] [2*]

* * * * *

FRANK H. WILEY,

called as a witness by the plaintiff, being first sworn, was examined and testified as follows:

The Clerk: Please state your name.

The Witness: Frank H. Wiley, W-i-l-e-y.

Direct Examination

By Mr. Neukom:

The clerk will please mark a box containing a group of bottles and a piece of paper containing attached to it some labels. Will this be either 1 or 2? It all involves one item, Count VII. [7]

The Clerk: This wrapped box, partly opened, marked Sample No. 30694-H, will be Government's 1 for iden-

(Testimony of Frank H. Wiley)

tification. The paper bearing the labels, among other words, contains the word "Pluri-B" twice, once on each label, and in the right-hand corner the number "256" will be Government's 2 for identification.

Q. By Mr. Neukom: Mr. Wiley, what is your business or occupation?

A. I am chief of the chemical section of the medical division of the Food and Drug Administration, Washington, D. C.

Q. You were so employed for about how long?

A. Since January 3, 1939.

Q. I call you "doctor." Will you please relate to the court, is that a degree in what?

A. That is a degree in biochemistry.

Q. Briefly, state your qualifications to the court.

A. I received a Bachelor and Master's degree from the University of Denver in 1925 and '26, respectively, then spent one year in a graduate school at the University of Illinois, and then three years in graduate school at the University of Michigan, where the degree of Doctor of Philosophy and Biological Chemistry was conferred upon me. I then spent about five years in research in the department of medicine at the University Hospital at Ann Arbor, Michigan. I was then [8] employed by the E. I. DuPont de Nemours Company for about five years, a little over five years, as biochemist in their institute of industry toxicology and, since January 3, 1939 I have been employed by the Food and Drug Administration.

Q. In the course of your duties did you have occasion to receive Government's Exhibit No. 1, a box containing a certain group of vials. Will you please inspect it and

(Testimony of Frank H. Wiley)

say if you see any identification of the markings of your initials or otherwise?

A. Yes; I did receive this box.

Q. You received it on or about what date?

A. If I may refer to my notes, I think my testimony might be more accurate.

Q. Yes; you may refer to your notes.

A. (After referring to notes.) I received this sample on July 23, 1946.

Q. And it had been mailed to you by one of the Food and Drug inspectors?

A. Yes; it had been mailed to the Food and Drug Administration in Washington by Inspector Kerr.

Q. Who opened the box? A. I opened the box.

Q. And you found it contained?

A. I found it contained six vials, six rubber- [9] stoppered vials, each bearing an official Food and Drug Administration seal. That seal was identified simply as being "sample 30694-H" and bore the date "7-12-46" and the name "Morris P. Kerr."

Q. The inspector? A. The inspector; yes sir.

Q. And did each of the vials have upon them a label?

A. Yes; to each vial was attached a label.

Q. Pasted upon it? A. Yes.

Q. I show you Government's Exhibit 2 for identification to which there seems to be appended two labels.

(Testimony of Frank H. Wiley)

Were those two of the labels that were on two of the six bottles?

A. These are two of the labels that were on the six bottles, that were removed in the course of the examination and I prepared them on this sheet.

Q. Now, when you first looked at these vials, the two that we have here, what happened to the other four?

A. Two of the vials were subsequently used by our division of micro-biology in a test of sterility; two of the vials were used by our department of pharmacology in testing for pyrogen.

Q. The two vials that are here as part of Government's Exhibit 1, did they remain closed as they are now?

A. Yes; they did. These vials are in the condition [10] in which I received them.

Q. Did you observe when you first received these vials and did you put them up to a light and observe whether or not they contained undissolved particles?

A. I did.

Q. Just briefly relate what you found.

Q. I found that both vials, or all six vials, as a matter of fact, were very badly contaminated with undissolved material; that is, they contained quite a quantity of material which was not in solution.

The Court: Did you see that with the naked eye?

The Witness: Yes.

(Testimony of Frank H. Wiley)

Mr. Neukom: I would like to offer into evidence Government's Exhibit 1 and pass to the court for observation the two vials in question.

The Clerk: 1 for identification in evidence.

The Court: Government's Exhibit 1 for identification is received into evidence.

Mr. Neukom: I would like to offer Government's 2 into evidence, which were the labels that were on two of the vials.

The Court: Exhibit 2 for identification received into evidence.

[GOVERNMENT'S EXHIBIT NO. 2]

30 cc STERILE SOLUTION No. 256
 PLURI-B

(Some factors of the B Complex)

For Intramuscular or Intravenous Use

EACH CC CONTAINS:

Thiamine Hydrochloride	50 Mgms.
Riboflavin	2 Mgms.
Pyridoxine Hydrochloride	10 Mgms.
Pantothenic Acid	10 Mgms.
Nicotinamide	50 Mgms.
Chlorobutanol (Chloroform deriv.)	1/12 gr.—0.005 Gm.

CAUTION: To be dispensed only by or on the
prescription of a physician.

PASADENA RESEARCH LABORATORIES, Inc.
Pasadena 8, Calif., U. S. A.

Lot No. 317

[Written]: #4 30694 H 7/12/46 MPK

(Government's Exhibit No. 2)

30 cc STERILE SOLUTION No. 256
 PLURI-B

(Some factors of the B Complex)

For Intramuscular or Intravenous Use

EACH CC CONTAINS:

Thiamine Hydrochloride	50 Mgms.
Riboflavin	2 Mgms.
Pyridoxine Hydrochloride	10 Mgms.
Pantothenic Acid	10 Mgms.
Nicotinamide	50 Mgms.
Chlorobutanol (Chloroform deriv.)	1/12 gr.—0.005 Gm.

CAUTION: To be dispensed only by or on the
prescription of a physician.

PASADENA RESEARCH LABORATORIES, Inc.
Pasadena 8, Calif., U. S. A.

Lot No. 317

[Written]: #5 30694 H 7/12/46 MPK

[Written]: U S 2 for ident. 30694-H 8-1-46 F.H.W.

Case No. 19223 Cr. U. S. vs. Pasadena Research
Laboratories, etc. U. S. Exhibit 2. Date 6/17/47. No.
2 in Evidence. Clerk, U. S. District Court, Sou. Dist. of
Calif. Louis J. Somers, Deputy Clerk.

No. 11690. United States Circuit Court of Appeals for
the Ninth Circuit. Filed Aug. 25, 1947. Paul P.
O'Brien, Clerk.

(Testimony of Frank H. Wiley)

The Clerk: So marked.

Mr. Neukom: Would your Honor like to have me hand you the vials now? [11]

The Court: Yes; if you will.

Q. By Mr. Neukom: Are you acquainted with the authority known as "Pharmacopoeia of the United States, twelfth edition"? A. I am.

Q. Are your views in accord with the views expressed in this authority with regard to the appearance of solutions or suspensions in sterile solutions? A. Yes.

Q. Is this book that I have referred to, edition No. 12, is that a standard work? A. It is.

Q. As a matter of fact it is recognized in the Food and Drug Act, is it not? A. That is true.

Mr. Neukom: I call your Honor's attention to many definitions in the Food and Drug Act, reference is had to the Pharmacopoeia.

Q. Is it the views of chemists in your position that the product or sterile solution for intravenous and intramuscular usage should or should not contain undissolved material?

A. I think perhaps such a conclusion would be outside of the field of responsibility of a chemist.

Q. I see. Are there further observations that you had [12] to make with regard to these two vials, or as to Government's Exhibit No. 1 as a result of your tests?

A. Shortly before coming to Los Angeles for this case, I re-examined the vials and found that they were still in about the same condition as regards the amount of undissolved material present.

Q. May I ask you about that? Pause at this point. Were the vials, when you examined them as of the date

(Testimony of Frank H. Wiley)

they were received, did they contain virtually the same amount of undissolved materials as they do now?

A. Yes. The amount of undissolved material there is about the same as it was when I originally examined it.

Q. In other words, it has not increased in any appreciable amount here as to your knowledge?

A. No.

Q. Do you have an opinion as to whether or not this undissolved material, as noted in this solution, was there at or about the date of June the 18, 1946, which was some several months, I believe—how long was it before you examined it?

A. The date of shipment was June 17th.

Q. June the 18th, 1946. And you examined it about—

A. I examined it on August 1st; so that would be about six weeks before I examined it.

Q. Do you have an opinion as to whether that undissolved [13] material was present as of the date June 18, 1946?

A. Yes. I—

Mr. Stick: Just a moment, your Honor. We object to that question, even though this man is an expert, unless it is shown as to what conditions this bottle was kept in or these vials, whether they were subject to any outside influences which could have affected them, whether the labels had been removed or whether anything had been done to change the condition of the solutions that were in the bottles between the time it was shipped and the time this gentleman saw them.

The Court: He testified that the bottle was sealed, did he not?

(Testimony of Frank H. Wiley)

Mr. Stick: It was sealed at the time it was picked up by the inspector on July 12th. This product was shipped June 18th, and between June 18th and July 12th, when it was picked up by the inspector, we have no evidence as to the conditions surrounding it, how long the inspector kept it and how and under what conditions it went back to Washington so that this man saw it on July 26th. We have no circumstances or no facts.

The Court: Well, strictly speaking, I suppose it would be necessary to have one of these original bottles opened by a chemist appointed by the court and have that chemist make a very minute analysis of the contents, and then express [14] his opinion as to whether or not that combination of substances in the bottle under those conditions would change in time, or whether there would be some precipitation inside the bottle or some other changes.

Mr. Stick: Yes. And also, that no outside influence of any kind affected the contents of that bottle; and that can only be determined by the evidence of the parties who had control of the bottle between the time when it was analyzed and the time when this gentleman received it and the time it was put in interstate commerce.

The Court: Well, of course, we have a bottle here which is said to be the original container. We have two of them in Exhibit 1 which are said to be original.

Mr. Neukom: They are still sealed, never been opened. I believe that is your testimony?

The Court: Unopened bottles.

Mr. Stick: That does not necessarily mean that the contents of that bottle cannot be affected.

The Court: No. My observation is this: It seems to me that, before anyone could express an opinion, he

(Testimony of Frank H. Wiley)

would have to take the contents of one of these bottles, it would have to be opened, he would have to say that he opened it, took the contents out and made an analysis, or did whatever was necessary to reach an informed opinion as an expert upon when that sediment or undissolved material came into [15] being, whether it was precipitated early or late, or whether it was in solution at the time it was placed in the bottle. I take it that a chemist can do that. I don't know.

But, can we take this witness' opinion, Mr. Neukom, based upon his examination of a bottle which had been opened and conceivably might have been tampered with or even the entire contents changed before he received it?

Mr. Neukom: Well, if that was the rule of law, you could never prosecute under the Food and Drug Act.

The Court: Oh, yes. Yes; you can take that bottle there, and the court will appoint a chemist if the court insists upon that type of proof. The court will appoint a chemist and the chemist can make the analysis, and we will give him the time that is necessary and he can come and express an opinion as to the contents of that bottle with respect to whatever is in there insoluble.

Mr. Neukom: Of course, my position is—may I express my opinion briefly?

The Court: Yes.

Mr. Neukom: Dr. Wiley tells me, and I believe that this would be his testimony, that he can form an opinion from observing this motherly matter or undissolved particles at the time he saw it six weeks after shipment, without even opening the bottle.

(Testimony of Frank H. Wiley)

The Court: If he can express an opinion as to one of [16] these bottles in Exhibit 1, that is a different matter.

Mr. Neukom: I understand he can express an opinion.

The Court: Suppose you inquire as to that opinion.

Mr. Neukom: Dr. Wiley—

Mr. Stick: My objection, then, is overruled?

The Court: Your objection is sustained to the question pending.

Mr. Stick: All right.

Q. By Mr. Neukom: Dr. Wiley, taking the two vials, part of Government's Exhibit No. 1, which I understand you examined about six weeks after the shipment in question here, from your knowledge of sterile solutions and from your observation of sterile solutions, your experience, are you able to express an opinion to this court as to whether or not the contents of those two vials, Government's Exhibit 1, did contain the undissolved particles you noticed there then as of the date they were shipped, namely, on or about June 18, 1946? Your answer is yes or no. A. Yes. [17]

* * * * *

Mr. Stick: He has an opinion.

Q. By Mr. Neukom: Now, waiting for the objection, what is your opinion?

Mr. Stick: I object to that, your Honor, upon the ground that until the conditions under which these bottles have existed or to which these bottles and contents have been subjected since the date that they were put into interstate commerce on June 18th must be before this witness before he can express an opinion as to whether

(Testimony of Frank H. Wiley)

or not the contents that are in there now were in the condition that it is now, going back to June 18th when it was shipped.

The Court: That may be so, Mr. Stick, but he says he has an opinion, and he says he has never opened that bottle. That is up to the experts. He can express an opinion. What you say may go to the weight of it, but not to the competency of it, I take it. Objection overruled.

Q. By Mr. Neukom: Will you please relate your opinion?

A. From experience with these materials and from general information of so-called supersaturated solutions, of which this is an example, I would say that this undissolved material was undoubtedly present on June 18th when the material was shipped. There is only one external factor of which I know that would hasten or increase the crystalization of this material, and that would be refrigeration. [18] I doubt very much if the mail bag in which this material was transmitted to Washington was in a refrigerator car.

Q. Then, in other words, coolness of, say, slightly above freezing, the temperature of the usual refrigerator, might hasten the cloudy condition?

A. It might hasten it if the crystalization had not already taken place.

Q. Normal temperatures—now, for instance, assuming that this product went where it became quite warm, and by that I will say up to 110 or 115, in your opinion, if it was sealed in those bottles here, would that have hastened the accumulation of the undissolved particles?

A. No; it would not.

(Testimony of Frank H. Wiley)

Q. Would it have any effect at all, in your opinion?

A. It might even have slowed up the appearance of those particles slightly, due to the increase of solubility at a higher temperature.

Q. In other words, heat retard and coolness might hasten?

A. That is right.

Q. I call to your attention, although I believe this is evidence, maybe, your Honor, in looking at the label did you note any caution as to how it should be retained or kept with regard to heat or cold?

A. There is no caution on this label as to conditions [19] under which the product should be stored.

Q. And, Dr. Wiley, a brown bottle such as that is in is a bottle that is proper to use, is it not, in retaining solutions?

A. Yes; this type of bottle is often used for the packaging of materials that are sensitive to the light.

Q. Or blue; it is to keep out unnecessary light, isn't that it?

A. That is it. That is true.

Mr. Neukom: That will be all.

The Court: The container in which that solution is found now is a proper container for the shipment of a sterile solution?

The Witness: Yes. Yes; it is a proper container.

Cross Examination

By Mr. Stick:

Q. Dr. Wiley, isn't it true that thiamin solutions, thiamine hydrochloride, have a tendency to precipitate?

A. It depends entirely upon the composition of your thiamin solution. If the thiamin used is not pure, there might be some impurities in the thiamin which will pre-

(Testimony of Frank H. Wiley)

precipitate out. However, a pure grade of thiamine hydrochloride will form a pure solution and remain clear.

Q. You spoke in your examination of a supersaturated [20] solution. What do you mean by that?

A. It is a solution which contains more of the material dissolved in the solvent than it would ordinarily hold; that is, materials are said to be soluble to the extent of so many grams per cubic centimeter. If you dissolve more material than that number of grams in a cubic centimeter of the solvent, the solution is said to be supersaturated.

Q. Was this a supersaturated solution in the vials that you have before you?

A. It was supersaturated in that it contained more riboflavin than you could ordinarily dissolve in that amount of fluid.

Q. Is riboflavin stable as to its remaining in solution?

A. If the amount dissolved is below the saturation point, I would say it was.

Q. With the formula that appears on these bottles, would you say that the thiamin and the riboflavin would have a tendency to precipitate?

A. The riboflavin would. I do not recall just how much thiamin there was in there or what the solubility of thiamin is at the moment.

Q. I will show you Government's Exhibit 2 for identification. Could you tell from looking at that? [21]

A. If you would permit me to refer also to USP to find the solubility of thiaminechloride, I think I could. (After examining data.) The label indicates that this preparation contains 50 milligrams of thiaminehydrochloride per cc; that is 5/100ths of a gram. United States

(Testimony of Frank H. Wiley)

Pharmacopoeia states that one gram of thiamine hydrochloride will dissolve in one cc of water. In other words, this preparation contained only about 1/20th of the amount of thiamine hydrochloride which you can dissolve in water, consequently it was not. If it was pure, thiaminehydrochloride don't precipitate out.

Q. Would the fact that other ingredients were dissolved in the same cubic centimeter of the contents have to do with its saturation?

A. That depends entirely upon the nature of the ingredients, of course.

Q. From the ingredients that are set forth in that formula?

A. I do not believe that the ingredients set forth on this label would cause the thiamine hydrochloride dissolved in this amount of water to precipitate.

The Court: By "this label" you are referring to Exhibit 2?

The Witness: Exhibit 2; yes.

Q. By Mr. Stick: All right. Now, what about [22] riboflavin?

A. The label in Exhibit 2 indicates that each cubic centimeter of this preparation contains two milligrams of riboflavin per cc. Riboflavin is soluble in water to the extent of about 1/10th of a milligram per cc. In other words, this solution is labeled to contain 20 times

(Testimony of Frank H. Wiley)

as much riboflavin as you can ordinarily dissolve in one cc of water.

Q. And that would have a tendency, then, to precipitate, would it not? A. It would; yes.

The Court: Did I understand you correctly that two milligrams of riboflavin in one cc of water would be approximately 20 times too much that which would dissolve in that quantity of water?

The Witness: That is 20 times as much as you could normally get in one cubic centimeter of water; yes. It might be possible to get that amount of riboflavin in water by heating it up and dissolving it. I am not sure exactly what the solubility of riboflavin at high temperatures is, but at room temperature that is 20 times the amount you would expect to stay in solution.

The Court: You would call that 20 times over-saturation?

The Witness: Yes; it could be called that.

Mr. Stick: That is all. [23]

Mr. Neukom: That is all, Doctor.

Mr. Stick: Pardon me. Your Honor, may I ask him just one more question?

Q. You did not see these vials until you saw them in Washington, is that right? A. That is true.

Q. You never saw any of them prior to that time?

A. No.

Mr. Stick: That is all.

Mr. Neukom: Dr. Thienes, please.

CLINTON H. THIENES,

called as a witness by plaintiff, being first sworn, was examined and testified as follows:

The Clerk: Please state your name.

The Witness: Clinton H. Thienes, T-h-i-e-n-e-s.

Direct Examination

By Mr. Neukom:

Q. Do you live in Los Angeles? A. Yes, sir.

Q. And your occupation?

A. I am a physician and I am also a professor of pharmacology at the University of Southern California medical school. [24]

Q. You are a graduate of what university or universities?

A. I have degrees Bachelor of Arts, Master of Arts, and Doctor of Medicine from the University of Oregon, and Doctor of Philosophy from Stanford University.

Q. You have how long been affiliated in the capacity that you have related with the University of Southern California, pharmacology?

A. I have been with the University of Southern California since 1929 and head of the Department of Pharmacology since 1931.

Q. And you are likewise practicing your profession here in the city? A. Yes; I am.

Q. Are you a member of any scientific societies, Doctor, medical societies?

A. I am a member of the American Society for Pharmacology and Experimental Therapeutics, of the Society for Experimental Biology in medicine, of the American Association for Advancement of Science, the American Medical Association, and the Los Angeles

(Testimony of Clinton H. Thienes)

Medical Association, the California Medical Association, Western Association of Industry, Physicians and Surgeons.

Q. You are not employed by the Federal Food and Drug, of course? [25] A. No; I am not.

Q. You have been retained as an expert in this case?

A. That is right.

Q. Doctor, are you familiar with the usage of sterile solutions for intramuscular or intravenous use as to their condition? Are you familiar with such solutions?

A. Yes.

Q. I will show you two vials from Government's Exhibit No. 1, and would like to ask you to put those up to the light and observe what you can see of the contents. Before doing that, Doctor, when a solution is injected into a person, it either goes into a muscular tissue or into a blood vein; isn't that true?

A. Or into the skin or just under the skin.

Q. But it can go into the blood vein, can it not?

A. That is right.

Q. And sterile solutions of such character as that—have you seen the formula of this product here?

A. I don't think I have.

Q. Will you look at Government's Exhibit No. 2?

A. These represent labels from two separate bottles of some type of preparation, I take it?

Q. Yes; that is my understanding of the testimony. They are both the same, I think, the two.

A. Yes. [26]

Q. Is such a solution, or a solution of materials, drugs, or whatever they are of that type, is that such

(Testimony of Clinton H. Thienes)

that might be used where it was injected in the blood stream? A. Yes.

Q. I note that the label says "for intravenous use."

A. Yes; and preparations of this general composition are used intravenously and intramuscularly.

Q. Doctor, you have examined the two vials there. Did you observe anything unusual?

A. There was considerable precipitate or undissolved material.

Q. In your opinion as a medical man, Doctor, would a solution containing undissolved material such as that be considered proper by physicians who adhere to the usual degree of care and caution, to use intravenously upon a human being? A. No; I would not.

Q. Doctor, if you were to inject into a person a solution which contains cloudy or undissolved particles such as you observe there, might there be any harm or any blockage of either the heart or blood stream if such particles clotted in some of the veins?

A. Particles of the size which I observe in these two vials are of sufficient size to block the smaller veins and capillaries. Some of these particles are large enough to block what we might call a fair-sized vein. [27]

Q. Might that cause harm?

A. And if injected as ordinarily injected, it would lodge in veins of the lung or, rather, in branches of the supplementary artery and cause blockage of the circulation in two parts of the lung. That might result in shock from just the sudden blocking of the vessel, and pain and subsequent infection may occur in such places.

(Testimony of Clinton H. Thienes)

Q. In your opinion would such a solution be proper—I think you did express an opinion.

A. No; such a solution would not be proper for intravenous injection.

Q. How about intramuscular?

A. It would not be proper for intramuscular injection.

The Court: Would the infection result from loss of blood supply?

The Witness: Well, from the loss of blood supply, the irritation set up. Primarily, the loss of blood supply reducing the resistance of the tissue.

Q. By Mr. Neukom: Doctor, would you expect and is it the consensus of opinion of practitioners who use intravenous or intramuscular solutions, sterile solutions, that such solution be free from undissolved particles?

A. Yes.

Q. You are familiar with the Pharmacopoeia of the United States, are you not? [28]

A. Yes, sir.

Q. You share the views that are expressed on page 221 of this authority? This is an authority, is it not?

A. I accept it as law.

Q. Referring to what I have marked: "Appearance of Solutions or suspensions," would you read that audibly and then state whether or not you share that view, that two brief paragraphs?

A. "Injections which are solutions of soluble medications must be clear, and free of any turbidity or undissolved material which can be detected readily without magnification when the solution is examined against black and white backgrounds with a bright light reflected from a 100-watt Mazda lamp or its equivalent.

(Testimony of Clinton H. Thienes)

“When preparing an injection containing suspended medicament, pass the drug through the standard sieve of at least 200-mesh or employ equivalent treatment in a colloid mill.”

Q. Do I understand that is likewise your view?

A. Yes.

Q. Doctor, in your opinion does the solution, as you now see it before you, meet the definition that is contained in the Pharmacopoeia?

A. No; it is my opinion that it does not. [29]

Mr. Neukom: That is all, Mr. Stick.

Cross Examination

By Mr. Stick:

Q. Are you familiar with this product called “Pluri-B” as a general product?

A. I don’t know what you mean by that question, sir. I have seen it—I have seen a product either with this name or a similar one in the case of representatives who have come to my office.

Q. And this Pluri-B, being this type of product, is manufactured by more than one concern, more than this defendant, to your knowledge?

A. Similar mixtures are manufactured; yes.

Q. Doctor, is it customary for a doctor to look at a bottle of solution from which he is going to take material for an injection to see whether it is free from suspended particles or undissolved material?

A. It is customary.

Q. And if a doctor were to look at either of those bottles and see that suspended material in it, would the doctor use it? A. No; not the average doctor.

(Testimony of Clinton H. Thienes)

Q. As a matter of fact you would not expect any doctor to use it if he saw particles of that kind in it? [30]

A. Yes; I think perhaps a doctor might.

Q. You think he might?

A. Some doctor might.

Q. How would he give that to the patient if he was giving a dose out of either of those bottles?

A. He would withdraw it with a syringe and needle and—

Q. That is, he would insert the needle into the bottle through the rubber diaphragm which acts as a cork in the top? A. That is right.

Q. And while it was in there, he would then draw out a certain quantity into his syringe? A. Yes, sir.

Q. And then he would withdraw the needle from the bottle and inject it into the patient?

A. That is right.

Q. Would those larger particles in there go through the needle of a syringe?

A. It depends on the size of the needle.

Q. All right. What size of needle is ordinarily used in that type of injection?

A. From an 18 to—from about a 22 to a 16-gauge.

Q. Would they pass through that, either of those?

A. Many of these particles would pass through at 22-gauge needle; yes.

Q. That is many of the smaller particles? [31]

A. Yes.

Q. But the larger ones would not?

A. I think the largest particles would probably not enter even a 16-gauge needle.

(Testimony of Clinton H. Thienes)

Q. Have you ever examined any of the so-called Pluri-B solutions that are on the market? Do you ever use them?

A. I presume by that term you mean B Complex solutions. "Pluri-B" I take it is a trade name applied to this one product, and not to all vitamin B complex products.

Q. All right; a solution similar to that; are you familiar with them and have you used them?

A. Yes.

Q. Did you find any undissolved particles in any of them that you used?

A. I don't recall of seeing any in any that I ever used.

Q. Did you ever examine carefully?

A. Oh, yes.

Q. In this Pharmacopoeia from which you read, you read this portion:—

Mr. Neukom: Page 221.

Q. By Mr. Stick: "When preparing an injection containing suspended medicaments"—
is that the way you pronounce it?

A. That is the right way. [32]

Q. —"pass the product through a standard sieve of at least 200-mesh or employ equivalent treatment in a colloid mill"? A. Yes, sir.

Q. Doesn't that recognize that there will be in suspension certain particles in injectable material?

A. Only in a very restricted number, sir.

Q. But it does recognize that they can be there?

A. It would seem so.

(Testimony of Clinton H. Thienes)

Q. And when they are there, it gives you a recommendation as to what to do to get rid of them; isn't that true?

A. It gives that recommendation to the manufacturers, and not to the doctor.

Q. That is not to the doctor? A. Oh, no.

Q. Do doctors have the Pharmacopoeia?

A. A few of them.

Q. Do you know anything about the precipitation of riboflavin in solution?

A. I know something about it.

Q. And of thiaminehydrochloride? A. Yes.

Q. Could you tell from the precipitate in those bottles whether that precipitate is either thiaminehydrochloride or riboflavin? [33]

A. No; I could not by just looking into the bottle this way. I would have to test it chemically.

Q. Do you know what the precipitate in those bottles is? A. No, sir.

Q. Have you ever seen those bottles prior to August the 1st of 1946? A. No.

Q. When did you first see them?

A. I don't know that I have seen them before this morning. I saw a couple of bottles yesterday, but I don't know that they were these two bottles.

(Testimony of Clinton H. Thienes)

Q. Would a 200-mesh sieve remove the particles that are in that solution if the solution were passed through it?

A. It would remove most of it. I think some of the particles would pass through.

Q. Would those that would pass through be harmful to inject?

A. If injected intravenously, yes; and even intramuscularly, they might.

Mr. Stick: They might. That is all.

Mr. Neukom: I have a couple of questions. [34]

Redirect Examination

By Mr. Neukom:

Q. Doctor, you note in Government's Exhibit No. 2 the size of the labels here, do you not? A. Yes, sir.

Q. If they were glued to the vials would they retard the doctor's ability to detect the particles?

A. It would make it difficult; yes.

Q. Doctor, does a busy practitioner use a solution of the B complex, of which this is, I understand you to say, of such a character, is it not?

A. It is a B complex mixture; yes.

* * * * *

The Court: Sustained. The answer is stricken.

Q. By Mr. Neukom: Doctor, in your opinion as a physician and surgeon, in purchasing a sterile solution for intravenous and intramuscular use would you expect the

(Testimony of Clinton H. Thienes)

solution to be free and clear from undissolved particles?

A. All except certain special preparations such as bismuth salts, which are used in medicine and are not soluble [35] but are in suspension. They are used with very special care.

Q. I am referring to the B complex?

A. But the B complex should be entirely free from perceptible matter.

Q. And that is the view of a practicing physician who is using such product, isn't it? A. That is true.

* * * * *

Recross Examination

By Mr. Stick:

Q. Doctor, isn't it a fact that many estrogenic substances have suspended particles in them and are used in injections?

A. You will have to define the meaning of "many" there.

Q. Have particles?

A. Some, but relatively infrequently used. Estrogenic preparations have suspended particles and these are used with very special care and are injected only intramuscularly.

Q. Doctor, isn't it true that any good doctor will [36] always use extra special care? A. Certainly. [37]

* * * * *

ARNOLD E. MASON,

called as a witness by plaintiff, being first sworn, was examined and testified as follows:

The Clerk: Please state your name.

The Witness: Arnold E. Mason.

Mr. Neukom: We are going to Count I now, your Honor.

Direct Examination

By Mr. Neukom:

Q. Were you at one time employed as a chemist or analyst by the Food and Drug Administration of Washington, D. C.? A. Yes, sir.

Q. And you are not now so employed, are you?

A. No; I am not.

Q. Just what is your employment at the present time?

A. At the present time I am employed as a pharmacologist with Crystal Laboratories, Syracuse, New York.

* * * * * * * * *

Q. In the fall of 1945 you were employed by the Food and Drug Administration as a chemist or pharmacologist? [38] A. Pharmacologist and analyst; yes.

Q. Give briefly your qualifications, your schooling, what you have done.

A. Received a Degree of Bachelor of Science from the University of Nebraska; Master of Science in Physiology from the University of Michigan. I have attended school part time in Washington, D. C., Georgetown University, working on a Degree of Doctor of Philosophy.

Q. You were employed by the Federal Food and Drug Administration as pharmacologist for about how long?

A. For about three years.

(Testimony of Arnold E. Mason)

Q. As a part of your duties, working under your superiors, did you have occasion to analyze various products that were submitted to you? A. Yes, sir.

Q. Did you have occasion in the fall of 1945 to conduct an analysis for the purpose of detecting the existence or lack of posterior pituitary in a product known as "Indoform"?

* * * * *

A. I ran an assay or tested that product on February 15, 1946.

Q. I will show you a vial here—

May the vial be marked Government's next in order for identification, and a sheet of paper which contains a label [39] be marked to follow for identification?

The Witness: There are code numbers on there.

Mr. Neukom: The numbers, the other writing on here, your Honor, is inspectors' initials and dates and things such as that, which is customary in a case of this kind.

The Clerk: This vial will be Government's 3 for identification and the label will be 4 for identification. The label bears the words "Sterile Indoform."

Q. By Mr. Neukom: Taking the vial, can you note a seal there bearing your initials and date and analysis?

A. Yes, sir. The date of my analysis is scratched into the vial with a diamond pencil.

Q. Right on the glass itself?

A. Right onto the glass.

Q. And what is the date, approximately?

A. The date, I believe, is hidden by one of these seals.

Q. What do your notes show?

* * * * *

(Testimony of Arnold E. Mason)

A. Among my notes, I have the original inspector's seal here, which indicates that I examined this on February 18, 1946.

Q. And that refreshes your memory as to the date?

A. Yes, sir. [40]

Q. You examined the contents of that vial, Government's Exhibit 3 for identification, for what substance, if any?

A. I examined it to determine whether it had the labelled quantity of posterior pituitary.

Q. First, give what you found, and then we will go over the manner of means used in determining. I note from the label, Government's Exhibit No. 4 for identification, there is an indication that this Sterile Indoform contains posterior pituitary 3 international units per each cc. Incidentally, what is a "cc" in laymen's terms, a cubic centimeter?

A. A cubic centimeter is a small quantity which is used by chemists to measure liquid.

Q. About 20 drops?

A. About 16 to 20 drops in laymen's language.

Q. And 3 international units of posterior pituitary in each cc. Now, Mr. Mason, after you had conducted your tests, which we will go into later, what amount of posterior pituitary did you find, if any, that existed in this product?

A. I found practically no posterior pituitary in that product, an almost immeasurable quantity.

Q. Now, this is a little process that you went into. Are you going to resume this afternoon, or shall I start in on this, your Honor? I was going to make a diagram

(Testimony of Arnold E. Mason)

or map of this. But first, did you use the uterus or some sub- [41] stance from guinea pigs?

A. I used the excised uterus of a virgin guinea pig, which is standard tissue to be used in conducting this test.

Q. And that is the accepted test?

A. That is accepted.

Q. Explain briefly to the court just what you do. Take a virgin guinea pig and kill it, I assume; and then go ahead and explain it.

A. An assay, as given in the United States Pharmacopoeia, states that you must use virgin female guinea pigs of a certain weight. The guinea pig is killed; the uterine horns are removed from the body—

Mr. Neukom: Speak up a little louder.

A. —and suspended in a solution which is somewhat analogous to the solution that that tissue is bathed in in the body, and kept at a temperature corresponding to body temperature of the animal. That tissue, then, when treated with certain substances, will react the same as it would while it is in the body, and by so reacting with a standard solution of known potency—

Q. Let us define our terms. You say “standard solution of known potency”?

A. A standard solution is a solution of posterior pituitary powder. The powder is made into a solution, and by “standard” I mean that the activity of that solution is known [42] to be such that each $\frac{1}{2}$ milligram contains one unit of posterior pituitary activity. The stand-

(Testimony of Arnold E. Mason)

ard powder is the same as the international standard powder, and the solution is made up by the analyst according to the form given in the United States Pharmacopeia. By determining what the excised tissue will do when it is treated with that standard solution, one can determine what any unknown solution will do by comparing the reaction of the unknown solution with the standard.

Q. Were the horns of the uterus of the guinea pig excised and cut and used within a short period of time after the death of the guinea pig?

A. They were removed from the body and within a matter of a very few seconds placed in this solution which the U.S.P. prescribes to be analogous to the fluid surrounding that tissue in the guinea pig.

Q. Do you have a gauge? When you suspend a portion of uterus do you have some device or gauge that displays the contraction or the relaxant, whatever it is, of the uterus muscle?

A. The uterine muscle is so suspended in a bath at a constant temperature and hooked to two levers such as that a recording can be made of the contraction of the uterus whenever it is caused to contract by posterior pituitary.

Q. Posterior pituitary does cause a contraction, is that right? [43]

A. It does cause a contraction.

Q. Of course, the absence of it would be negligible in the spasm of the contraction of the uterus?

A. That is right.

(Testimony of Arnold E. Mason)

Q. Is that uterus in such a condition that it will also still show a little movement even though it was just in plain water? I mean is there some movement upon your machine that you use to gauge it with?

A. The uterus must be kept in the solution prescribed in the U.S.P. to remain alive. If it is not kept in the solution, it cannot be used in this assay. While it is in that solution it will have some automatic contractions.

Q. And did you endeavor to, and is it your opinion, that you adhered to the accepted mode of making this test?

A. Yes, sir.

Q. And did you have a cycle made showing the contraction of this particular test?

A. I have made a tracing showing contractions of this particular test.

Q. The tracing machine does something similar to an electric electrocardiograph machine or a barometer reading on a needle, is that right?

A. Yes, sir.

Q. Do you happen to have that one here?

A. The tracing of this particular test is the bottom [44] tracing.

Mr. Neukom: May this be marked for identification?
Counsel has not seen it.

The Clerk: Marked 5 for identification.

Mr. Neukom: I would like to offer into evidence Government's 3 and 4, so I do not forget to make my offer, unless there is some objection to them.

The Court: Exhibits 3 and 4 for identification are received into evidence. [45]

[GOVERNMENT'S EXHIBIT NO. 4]

30 cc Vial

STERILE

No. 92

INDOFORM

EACH CC CONTAINS:

Suprarenal Cortex 30 grs.	Whole Ovarian	40 grs.
Anterior Pituitary 30 grs.	Thymus Substance	15 grs.
Posterior Pituitary	Thyroid Substance	1 gr.
3 Int'l Units	Lymphatic Substance	5 grs.

Preserved with Chlorobutanol (Chloroform Derivative)
0.5% (w/v) and Tricresol 0.5% (v/v)

This preparation does not contain any known
therapeutically useful constituent.

CAUTION: To be used only by or on the
prescription of a physician.

PASADENA RESEARCH LABORATORIES, Inc.
Pasadena 8, Calif., U. S. A.

Lot No. 728

[Written]: PD-12694 27131-H 728 2-18-46 R. E.
Mason 4 for ident.

Case No. 19223. U. S. vs. Pasadena Research Labora-
tories. U. S. Exhibit 4. Date 6/17/47. No. 4 Identifi-
cation. Date 6/17/47. No. 4 in Evidence. Clerk, U. S.
District Court, Sou. Dist. of Calif. L. J. Somers, Deputy
Clerk.

No. 11690. United States Circuit Court of Appeals for
the Ninth Circuit. Filed Aug. 25, 1947. Paul P.
O'Brien, Clerk.

(Testimony of Arnold E. Mason)

* * * * *

Direct Examination (Resumed)

By Mr. Neukom:

Q. Mr. Mason, you were testifying with regard to Counts I and II, the product known as "Indoform," a trade name, and with regard to posterior pituitary, the difference or lack of sameness of the product. You had told us about the test which you had performed in conjunction with the uterus of the guinea pig. In conjunction with that test which you performed was there a graph or a sort of a picture made as you were running some of the tests? A. There was.

Q. I show you Government's Exhibit No. 5 for identification and ask you if that is the original graph itself of a portion of the test of the product involved here that you were testing? A. That is.

Q. Now, I have marked and put a little—I don't know [47] what they call them—a little circular white object on one item. Immediately below that, is that a display of one of the tests that you conducted?

A. That is a display of one.

Q. I put this little white arrow, piece of paper I have fastened on there, and does that indicate a portion of the other test? A. It does.

Q. All of the other lines and graphs that are on there, with the exception of the two I have indicated, have nothing to do with this particular product, is that correct?

A. No; that is right.

Q. They were run on the same type sheet?

A. That is right.

(Testimony of Arnold E. Mason)

Q. About the same time, of other products?

A. That is right.

Q. Just explain to the court what you did in running the tests of this product to ascertain whether it has posterior pituitary upon the horns of the uterus as you had it suspended. Did you use some other substance in the comparisons you made; and if the court wants you to, you indicate there on that graph the results?

A. In the first place, the guinea pig uterus is considered an animal tissue which will show quantitatively the amount of pituitary, posterior pituitary, which is given to it. [48] A standard solution of posterior pituitary is made up from a reference standard powder, a United States Pharmacopoeia reference standard powder, which is identical with international posterior pituitary powder.

This reference standard solution is then used to tell to what extent the uterus will contract with a given amount of standard solution. We want to know how much the uterus will contract with a given amount of standard solution. We can then give various doses of any unknown solution containing the posterior pituitary, and by comparing the reaction obtained from the standard solution and the reaction obtained from the unknown sample it is possible to calculate how many units of posterior pituitary are in the unknown preparation.

Q. Or its lack?

A. Or its lack. If there is no reaction or little reaction, it indicates that there is not an amount equivalent to the standard.

(Testimony of Arnold E. Mason)

Q. In this instance how strong was your standard; what was the gauge that you used?

A. A standard solution is made in ampules such that it contains two units of activity per cubic centimeter.

Q. Of posterior pituitary?

A. Of posterior pituitary reference standard.

Q. All right. Now, show to the court this particular item that I have the little white circle over. [49]

I have shown this to counsel prior, your Honor, and counsel wishes to follow.

Will you explain this little item, this graph here, just what was occurring? Was there a needle running on this black sheet of paper, Government's Exhibit 5?

A. Is it possible to use a blackboard?

Q. Yes; if that helps.

(Witness diagrams on blackboard.)

The Court: You are referring to the graph and the words and figures opposite that appear in the lower left corner?

The Witness: Lower right-hand.

The Court: Oh, it is the lower right-hand—

The Witness: Yes.

The Court: —corner of Government's Exhibit 5 for identification?

The Witness: That is right.

This will be a glass jar, chamber of some sort, and to make this drawing accurate, inside of this is another chamber. This is filled up with water which is kept at a certain temperature.

The Court: That is the outer container?

(Testimony of Arnold E. Mason)

The Witness: That is the outer container. The inner container is marked to contain a definite amount of solution which is prescribed by the United States Pharmacopoeia to be used in this assay. The solution, which is a governmental [50] solution for the muscle—the muscle is suspended in this solution and is held at the bottom by means of a hook.

The Court: Now, that is the uterine muscle?

The Witness: The uterine muscle. Another hook is placed in the top of the uterus muscle and a string is attached, going up and out of this bath, we might call it, and attached to a lever. This lever will be placed here. When pituitary solutions are added to the bath, this inner bath, it causes the muscle to contract or shorten. As the muscle shortens it pulls on this lever and the lever will go up. This lever has a pointer on it and is touching a drum, and that drum is a piece of paper which has been smoked by means of bubbling benzine through natural gas. Therefore, every time this lever goes up and down again it makes a scratch mark on the paper.

The Court: The recording needle is at the one end of the lever, is that right?

The Witness: That is right; recording the action of this muscle. Then when this paper is filled up or we are done with that particular work, the paper is removed and run through shellac for permanent record.

Q. By Mr. Neukom: And that is Government's Exhibit 5 for identification?

A. That is Government's Exhibit 5 for identification. In that right-hand corner of this exhibit, this is what has [51] happened.

(Testimony of Arnold E. Mason)

Q. Explain the time element as you do this, too, please.

A. All right. The muscle is attached here. It takes sometime for it to relax and to become normal after removing it from the body.

We will assume that this drum is moving constantly very slowly. If the drum is moving and this pointer is at this point on the drum, it will get a line. However, it is not usually a straight line because there is some constant automatic contracting of this muscle, including the uterine muscle. We may go along like this and get very little jog in that line. At this point in the record, to use the record for an example, at this immediate point the record is labeled: 1-B, one-half or five-tenths cubic centimeter, S_1 . " S_1 " indicates on this record the first solution of standard reference posterior pituitary that I had used in this test.

Then it says: 1-50 there. The standard preparation, as I mentioned a while ago, contains two U.S.P. units per cubic centimeter.

The guinea pig uterus is so sensitive to posterior pituitary activity that it is necessary to dilute that. This standard has been diluted 50 times. In other words, 1 cc of standard solution is diluted to 50 ccs with physiological salt solution. [52]

That has a time on the record, "12:42". Then there is another figure there, "13.5".

At this point a half a cc of standard preparation, diluted 50 times, is added to the bath. The muscle contracts; it contracts and, from experience, it is possible to tell when it is done contracting. As it is done contracting, the lever is lifted off of the drum, because as

(Testimony of Arnold E. Mason)

soon as it is done contracting it is removed. The internal muscle bath—

The Court: You mean the inner chamber—

A. The inner chamber.

The Court: —containing the muscle?

The Witness: That is right; has a tube, so that everything can be sucked out of that inner chamber. The muscle is washed with the normal bath so that it is not affected by any posterior pituitary solution.

The Court: By that do you mean that when you reach the point where the muscle contracts once, and at the time you estimate that that process, that first contraction, has reached its limits, you lift the needle, then drain the inner container, wash the muscle and start all over again; is that it?

The Witness: That is right.

The Court: And repeat the same process?

The Witness: The only reason the needle is lifted is because, if it is not lifted, when this chamber is drained and refilled the needle will go all over and make a rather [53] smudgy record.

Then as the chamber is refilled with fresh solution containing no pituitary activity, the muscle relaxes in a fashion similar to that and shows some more of these automatic contractions.

The Court: In other words, you have a down graph?

The Witness: That is right.

The Court: From the contraction you have, indicates that is a down graph?

The Witness: That is right.

This "13.5" represents millimeters that the muscle has contracted on the graph.

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Then this muscle has relaxed at this point and is ready again to show activity when pituitary solution is given to it. That is a period of 12 minutes there.

The next thing that appears on the record—

The Court: Is that always so, 12 minutes?

The Witness: 10 to 15 minutes. In 90 per cent of the tissues used, uterus muscles used, it will be 12 minutes.

The next thing on this record is labeled "2-B". "2-B" merely indicates a—

The Court: A repetition of the same experiment?

The Witness: Indicates the next step in this experiment. This is the first step. "2" represents the second step in this particular record. The "B" indicates the record on the [54] lower half, the tracings on the lower-half of this record.

"A" is the top half.

Here this muscle was given a half a cc of 12694, which is a number which has been assigned to a sample in the Division of Pharmacology, Food and Drug Administration, by that division, and that number corresponds with a Government number of the sample which has been assigned to it by an inspector.

The Court: Let me see if I am clear. "1-B" represents the test with the standard solution?

The Witness: That is right.

The Court: Now, "2-B" is to represent the test with the solution that is under investigation?

The Witness: That is right. This number is for my own identification of that particular sample.

Then I have "fs." here, and there is another record of time here, "12:54", which indicates that that was

(Testimony of Arnold E. Mason)

12 minutes after the standard solution was given. There is no record of any contraction.

This is about what the record looks like, I believe. That was left in there, the sample, half a cc, and this sample was left in the bath surrounding the uterine muscle for a time equivalent to the time it was in under when the standard solution was given.

Q. By Mr. Neukom: Under "1-B"?

A. Under "1-B". No reaction occurred. So, again, the [55] muscle bath was washed, the muscle was washed, in other words, and the muscle showed this relaxation again.

At "3-B" the same test of standard pituitary solution was given as at 1-B.

Mr. Neukom: Writing down figures on the black-board.

The Court: In other words, you repeated the test with the standard solution?

The Witness: Repeated it.

The Court: To ascertain if the muscle would still react to that solution?

The Witness: To be certain that the muscle was not dead, so to speak. Something like this happened: The muscle showed it was going to relax, and again it was washed out and returned to normal. Now—

The Court: What relaxation did it show? What contraction did the muscle show the second time you subjected it to the standard solution?

The Witness: It contracted a little more than it did the first time, $16\frac{1}{2}$ millimeters, whereas in the first case it contracted $13\frac{1}{2}$, the difference of 3 millimeters. The reason for that is probably that it has actually had a

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long rest here, longer than 12 minutes, since there was little or no activity shown up to this point.

The Court: By "long rest" you mean a long rest between the first application of standard solution and the second [56] application of standard solution?

The Witness: That is right. The standard solution "S," is made from a preparation containing two units per cubic centimeter. The 12694—

The Court: That is the solution under investigation?

The Witness: Under investigation, was labeled to contain 3 units per cubic centimeter. The standard solution, in order to be used, had to be diluted 50 times. This one had to be diluted 50 times because the muscle was that sensitive to pituitary.

The Court: Just a moment. Let me understand that. You mean in order to make a test you had to dilute it?

The Witness: In order to make a test.

The Court: You diluted it down to—

The Witness: This would have been—

The Court: —what percentage of units per centimeter?

The Witness: This would have been diluted down to point—this reference, ".04".

The Court: Cubic centimeter?

The Witness: Units per cubic centimeter. It would be 1-50 cc to .04 units.

The Court: Four one-hundredths of a unit, is that it?

The Witness: Yes; four one-hundredths of a unit. The solution under investigation should have been diluted a corresponding amount and should have given a contraction at a [57] corresponding height in order to contain the labeled amount of three units per cubic centimeter.

(Testimony of Arnold E. Mason)

However, in this test, as you can see, it was not diluted at all; it was used full strength and it still does not give a reaction. In other words, it was over 50 times as strong as the standard and still did not give a reaction. It was impossible to give enough of it to cause the contraction equivalent to the standard.

The Court: The solution under investigation is labeled to contain 50 per cent more in strength per cubic centimeter?

The Witness: That is right; or three units per cubic centimeter, and was not diluted at all, whereas the standard was diluted 50 times.

Q. By Mr. Neukom: Mr. Mason, you conducted this examination on what date? What was the date there?

A. February 18, 1940.

Q. Let us assume that this product was shipped on September 17, 1945, which is a matter of around five months, is it not, or thereabouts?

A. That is right.

Q. Is posterior pituitary a stable product?

A. It is very stable except at excessively high temperatures.

Q. Except at what?

A. Except at excessively high temperatures. [58]

The Court: What do you mean by "excessively high temperatures"?

The Witness: A temperature of boiling of a fairly long time, say, a few hours.

The Court: Translate that into degrees.

The Witness: 212 degrees Fahrenheit or 100 degrees Centigrade.

The Court: Or better?

(Testimony of Arnold E. Mason)

The Witness: Or better, for, say, five or six hours, then it will break down.

Q. By Mr. Neukom: In normally warm temperatures, even up to 120, like may occur in the desert, that would not affect it, would it?

A. It would not affect it.

Q. When I asked you if it is stable, does that also mean that it continues its effectiveness for many months and even years? A. Yes, sir.

Q. Now, with that in mind, have you an opinion as to whether or not the product that you examined, known here as "Indoform", whether or not it contained posterior pituitary in three international units?

A. It did not.

Q. Did it contain any posterior pituitary or, if any, approximately in what amount? [59]

A. I would say an amount which is not measurable, if any.

Q. Did it, in your opinion, contain any posterior pituitary at the time it was shipped on September 17, 1945?

Mr. Stick: I object to that as a matter that cannot be testified to by this gentleman, unless all of the conditions and factors under which this matter was kept, handled and existed between the time when it was shipped by the defendant to the time when he first saw it is also before him.

The Court: That is the ultimate fact to determine, is it not?

Mr. Neukom: Yes, your Honor.

The Court: Objection sustained.

Mr. Neukom: May I be heard? If that was the rule, your Honor, then he could not express an opinion as to

(Testimony of Arnold E. Mason)

whether or not the product that he examined did or did not contain a certain amount as of such and such a date, and we would not have any Food and Drug cases.

The Court: He can cover and has covered it.

Mr. Neukom: Well, except he has not expressed a fact opinion, your Honor.

The Court: But it seems to me it goes one degree beyond what an expert or any witness should be permitted or competent to say, and that is: Did the defendant commit the offense.

Mr. Neukom: Well, I do not exactly agree with you. It [60] would be so if we were going to evade a factual matter which was not susceptible of expert opinion.

Now, if we pick up a piece of gold today and a man says that it is so many carats of gold, if he is a metallurgist or knows something about it, why, he would be privileged to say that a year back it was 18 carat, too.

The Court: Yes; I take it that he might say in response to a hypothetical question, assuming that it was not subjected to excessively high temperatures which you have described, assuming it was not diluted, assuming that it was in the same physical condition as it was when you examined it, in your opinion, was—

Mr. Neukom: Then I will reframe it in this manner. I had thought that I had covered it by my other questions and, therefore, had not propounded the assumption question.

Q. Assuming, Mr. Mason, that this product was not exposed to excessive temperatures, that is to say, that you said was 212 degrees is the destructive temperature; and assuming the product was handled in a normal and careful manner, retained in the bottle, as Government's

(Testimony of Arnold E. Mason)

Exhibit No. 4, I believe; assuming which bottle you opened and conducted the test as you have testified; and, with the assumption of what you found or did not find at that time, have you an opinion as to whether or not this product contained three international units of posterior pituitary on September 17, 1945? [61]

Mr. Stick: The same objection.

The Court: Overruled.

A. It is my opinion that the product could not have contained three units of posterior pituitary per cubic centimeter on September 17, 1945.

Q. By Mr. Neukom: Now assuming that all that you have testified to here and the explanations you have given, what is your opinion, carrying on the assumptions that I have enumerated—what is your opinion as to the amount, if any, of posterior pituitary was in the product on or about September 17, 1945?

A. On that date, September 17, 1945, it is my opinion that there was a quantity of posterior pituitary present which was not measurable by the standard methods of measuring it or there was none.

Mr. Stick: Pardon me. That is under the same conditions as in your first question?

Mr. Neukom: Yes; assuming.

A. Assuming that it is kept under normal conditions.

Q. I might ask, further, is posterior pituitary required to be kept in an ice box?

A. I do not remember that statement on the label of this sample.

Q. Well, assuming that this—well, that is a matter for the court. When you looked at the label on this

(Testimony of Arnold E. Mason)

particular sample 4, did you note any caution or comment as to the mode of [62] keeping this product?

A. There is no statement regarding the storage of this product.

The Court: That is exhibit?

Mr. Neukom: 4, your Honor, in evidence.

Q. But, in your opinion—I am asking you your opinion as to whether or not posterior pituitary—you have stated that it breaks down at about 212 degrees, is that correct? A. That is right; it may.

Q. Well, under that, does it have a tendency to break down and lose its efficacy? A. It does not.

Q. Did you add anything to this product or substitute anything to the bottle in conducting your tests?

A. No; I did not.

Q. And after you had concluded your tests of this bottle, Government's Exhibit 3, what did you do with the bottle then?

A. After conducting the test, the bottle was replaced in a locked refrigerator until the next day; then I wrapped it and put a seal on it and it was sent to San Francisco.

Q. You caused it to be sent as a part of your official duties, is that correct? A. Yes, sir.

Q. To the analysts in San Francisco? [63]

A. Yes, sir.

Q. And this Government's Exhibit No. 3, does it have one of the seals on there with your initials?

A. This has the seal on it that I originally put on the package that the bottle was in.

Q. Your initials appear on there?

A. My name; yes, sir.

(Testimony of Arnold E. Mason)

Mr. Neukom: Under your name. I would like to offer into evidence Government's Exhibit No. 5 for identification, but with the understanding that the other graph marks, other than as indicated, have no bearing on the case. Those constitute part of another test.

The Court: Exhibit 5 for identification received into evidence.

Mr. Neukom: That is all.

The Court: At the time you first received this bottle, Exhibit 3, how was the top of it sealed, if it was sealed? Did it contain a cork?

The Witness: As I recollect, it contained a rubber stopper. I cannot be certain without again looking at the bottle. The same stopper would still be on it.

The Court: Mr. Clerk, will you hand the exhibit to the witness, please?

The Witness: It contains a rubber stopper, your Honor.

The Court: Is that a rubber stopper similar to a cork, [64] what we call commonly a cork?

The Witness: Yes. Part of the rubber stopper serves as a cork and goes down inside the neck of the bottle.

The Court: Was that cork sealed into the bottle in any way?

The Witness: I do not remember whether it was sealed into the bottle or not. It has the same type of rubber stopper that is commonly on such preparations.

* * * * *

The Court: Mr. Clerk, will you exhibit or show the witness the containers in Exhibit 1, the two bottles in Exhibit 1?

(The clerk exhibits said bottles to the witness.)

(Testimony of Arnold E. Mason)

The Court: Was the bottle, Exhibit 3, at the time you received it corked or closed and sealed in the same manner or a similar manner?

The Witness: It was sealed in the same manner as Exhibit No. 1.

The Court: As those bottles, those two bottles?

The Witness: As those two bottles.

The Court: That is all I have.

Cross Examination

By Mr. Stick:

Q. Mr. Mason, this seal that you speak about on these [65] bottles and call a cork is actually a material which clamps around the outside and has a small rubber diaphragm, thin diaphragm, in the center; isn't that true?

A. The rubber cork goes down into the neck of the bottle for a short distance, folds around the outside of the bottle, then is sealed with a plastic seal.

Q. And the center of the cork is a very thin membrane of rubber; isn't that true?

A. That may only be determined in that particular cork by cutting the cork up.

Q. Isn't it true that they have that so the hypodermic needle can be run through the center diaphragm and the solution taken out? A. Yes; that is usual.

Q. Isn't it true that that is the standard and usual practice?

A. That is the standard practice of using a needle.

The Court: Did this Exhibit 3, when you received it, the bottle, appear to be so corked?

The Witness: Yes, sir.

The Court: As counsel has just described it?

(Testimony of Arnold E. Mason)

The Witness: Yes, sir.

The Court: That is, corked and sealed?

The Witness: Corked and sealed.

Q. By Mr. Stick: Generally, the type of cork would be such as the type of cork that is on the bottle I now hand [66] you to look at?

Mr. Neukom: May that be identified as, maybe, defendants' A, your Honor?

The Court: Yes; it may be marked for identification as Defendants' Exhibit A. A. Yes, sir.

Q. By Mr. Stick: And there is in the top of that a small depression which is the part where the needle is usually inserted for the purpose of withdrawing a part of the contents; is that not true?

A. That is true.

The Court: Now, did this bottle, Exhibit 3, at the time you first saw it appear to be corked and sealed in the same manner as Defendants' A for identification?

The Witness: In the same or a similar manner.

Q. By Mr. Stick: Did you make any examination of the cork that was on the bottle which you investigated as to its condition, or whether it had been used or whether it had been punctured by a needle? Did you make any independent investigation of that point?

A. No; I did not examine the cork in that fashion.

Q. Now, Mr. Mason, in making this test that you have made and explained here, you used the tests or followed the test that is laid down in the Pharmacopoeia of the United States of America? [67]

A. I followed that procedure.

(Testimony of Arnold E. Mason)

Q. Now, what is the accuracy of that test?

A. The accuracy of that test, as is given in the United States Pharmacopoeia, is plus or minus 20 per cent.

Q. Plus or minus 20 per cent?

The Court: By that, do you mean that you should allow to that extent, 20 per cent for error?

The Witness: That is correct.

The Court: You tested and found a certain number of units, according to your test, and you should allow 20 per cent more, is that it?

The Witness: If I had tested a preparation and calculated it on a percentage basis, and it came out 82 per cent of labeled potency, I would assume that the 18 per cent—that it could have been 100 per cent, and that the 18 per cent difference might be due to errors in the assay, which are possible, and to the variation in the animal tissue.

Q. By Mr. Stick: Would you state again just how you prepared this standard solution that you made?

A. A reference standard posterior pituitary powder is received from the U. S. Pharmacopoeial committee on revision in a sealed ampule. Upon immediately receiving that powder it is dated, initialed, and placed in an ice box. Whenever a standard solution to be used in assay is to be prepared, the powder is removed from the ice box, the ampule broken, and the [68] powder carefully weighed and made into a solution according to the directions in the United States Pharmacopoeia.

That solution is then sterilized and put into hard glass ampules, the ampules sealed, labeled, and placed again in a locked ice box. The solution is made up to contain two U.S.P. units per cubic centimeter. Then the solution

(Testimony of Arnold E. Mason)

in this case is made up by two individuals to insure accuracy.

Q. How do you mean made up by two individuals?

A. There were two individuals present while the standard solutions were being made up.

Q. Who made them up?

A. Dr. Vos, in Washington, D. C., and myself.

Q. Were you both present at the time?

A. We were both present.

Q. Why do you place these solutions, this powder, in an ice box?

A. Why did I place it in the ice box?

Q. Yes.

A. The powder is placed in the ice box because that is the one place we have a key. The ice box is locked. All standard preparations are kept in that place under lock so they cannot be tampered with by anyone except the person using them.

Q. What is the temperature of that ice box?

A. I couldn't say exactly. It is an ordinary refrigerator- [69] ator.

Q. This standard solution that you made, then contained only water and this posterior pituitary powder?

A. The standard solution also contains a very slight amount of acid.

Q. What kind of acid?

A. It contains—it is made up with the standard powder and 25 one-hundredths per cent of acetate acid.

Q. Is that according to the test here in the Pharmacopoeia?

A. That is according to the United States Pharmacopoeia directions.

(Testimony of Arnold E. Mason)

Q. Then, water, pituitary powder and the acetate are all that there was in your standard solution?

A. That is correct.

Mr. Stick: That is all.

Redirect Examination

By Mr. Neukom:

Q. You testified that you sealed the Government's Exhibit No. 3 and then caused it to be sent on to San Francisco; was that your testimony? A. Yes, sir.

Q. And you placed a seal on it, but now you see underneath another seal, is that correct? [70]

A. Yes; I do.

Q. Of course, you don't know how that got there only by surmise, is that correct? A. That is right.

Q. Just one question about the needle here. To what extent, in your opinion, would the needle have been caused to raise from the contraction had this product designated here as "2-B", the product here involved, had it contained three international units and you had made the test of full strength—which you did make it of full strength, I understand, is that right?

A. Yes, sir. The contraction would have gone as high as the muscle was able to contract; that is, the lever would have gone as high as the muscle could have made it go; the maximum contraction which was possible for that muscle would have occurred.

Q. Assuming that the contraction on the standard here was about five inches, in point of inches, and assum-

(Testimony of Arnold E. Mason)

ing on your diagram, have you an opinion as to how far it would have gone?

A. It certainly would have gone over five; it would have gone any place from 10 to 25 inches.

Q. Your needle reading? A. Yes, sir.

Mr. Neukom: That is all. [71]

* * * * *

The Court: That is all, Mr. Mason.

Mr. Neukom: Mr. Buell.

ANDREW G. BUELL,

called as a witness by plaintiff, being first sworn, was examined and testified as follows:

The Clerk: What is your name, sir?

The Witness: Andrew G. Buell, B-u-e-l-l.

Direct Examination

By Mr. Neukom:

Q. What is your business or occupation?

A. I am a chemist for the United States Food and Drug Administration, stationed at San Francisco.

Q. Were you such in February of last year?

A. Yes, sir.

Q. You have been practicing your profession for about how long? A. About 21 years.

Q. You are a graduate of what school? [72]

A. University of Nebraska.

Q. Specialized in Chemistry there?

A. Yes, sir.

Q. And since then what?

A. I was employed by the United States Patent Office for a year and half, and since then continuously in the United States Food and Drug Administration.

(Testimony of Andrew G. Buell)

Q. You have had occasion, from day to day and week to week all this time, to conduct analyses and examine products for the Government, is that correct?

A. Yes, sir.

Q. In the course of your duties did you receive, being transmitted to you from Mr. Mason, what now has been marked as Government's Exhibit 3 in evidence? And I would like to have you look at the seal on that bottle, the lower seal.

A. Yes, sir; that is my seal there.

Q. And first, so we can take this seal off and see what this cork is like, just tell us this: You did conduct an investigation or an examination of that product after you received it, is that correct?

A. Yes; I did sir.

Q. And when that produce came to you did it have a seal on it?

A. Yes; it had this top seal of Analyst Mason.

Q. That was glued on there in similar fashion—am I [73] correct—as the seal which is now adhered to and glued to the bottle, is that right?

A. No; that seal—the bottle was wrapped in paper.

Q. Oh, yes.

A. And the paper was sealed.

Q. So that before you could get to the bottle you had to break the seal that I have this rubber band around, the top of the neck of this bottle, is that correct?

A. Yes; I had to break Analyst Mason's seal to get at the bottle.

Q. And you did open that package yourself, is that correct?

A. Yes, sir.

Q. And what is about the date that you did do that?

A. On March 27, 1946.

(Testimony of Andrew G. Buell)

Q. Then, shortly after that, after you had conducted your investigation, which I am going to go into here in a moment, did you then reseal the remainder of the contents of this bottle?

A. Yes. After I made my examination, I immediately put my seal on the bottle.

Q. And that is the seal which now seals the bottle?

A. Yes; and dated March 28, the day after I examined it.

Mr. Neukom: Has counsel any objections to my removing [74] the little top part of this seal so that we can see what type of rubber stopper there is?

Mr. Stick: None whatever.

Mr. Neukom: The record may show that I have opened and bent back the seal placed on by Mr. Buell.

The Court: On Exhibit 3?

Mr. Neukom: On Exhibit 3, your Honor. And I will put a rubber band around Mr. Mason's seal, which is a part of the same exhibit.

Q. When you received the bottle did it have that character of stopper that you see there?

A. Yes; it is in the identical condition that it was when I received it.

Q. And before you took any out of the bottle—or, how did you take it out? Did you have a syringe and pull it out in that manner?

A. No. I just removed the stopper and took my portion for an analysis with a pipette.

Q. With a what? A. With a pipette.

(Testimony of Andrew G. Buell)

Q. Did you conduct an analysis upon this product after you had received it to ascertain what, if any, thyroid substance it had?

A. Yes; I examined it for thyroid content.

Q. And after you had given it the test, which you will [75] later relate, what, if any, thyroid did you find this substance had, this Indoform had?

A. There was no thyroid present whatsoever.

Q. Now, will you relate to the court the means that you used to endeavor to ascertain whether or not there was any thyroid in the substance?

A. Well, I made a quantitative determination of organically combined iodine.

* * * * *

Q. By Mr. Neukom: Incidentally, is there any correlation between iodine and thyroid?

A. The activity of thyroid depends on the organically combined iodine present in the thyroid.

Q. All right. Now, will you tell the court just what you did?

A. Well, I withdrew 15 cubic centimeters of the product.

Q. From Government's Exhibit 3 here?

A. From Government's Exhibit 3, and determined the iodine by the Elmslee-Caldwell method. [76]

* * * * *

Q. By Mr. Neukom: And what is that method?

A. Well, that is the most acceptable method for the determination of iodine.

(Testimony of Andrew G. Buell)

Q. Now, you keep saying "iodine"; so let us have the explanation between why you were looking for iodine when here we are looking for thyroid.

A. The activity of thyroid depends on the organically combined iodine present. The iodine in thyroid is present as the di-iodo-tyrosine, and also as thyroxine.

The Court: What is that first word you used?

The Witness: Di-iodo-tyrosine.

The Court: In other words, a thyroid tablet or a thyroid medicine contains iodine, is that it?

The Witness: That is right; organically combined iodine. Yes, sir, your Honor.

The Court: What else would it contain?

The Witness: Well, to produce the thyroid, the thyroid glands of sheep and hogs taken and the connective fat tissue is cut off.

Mr. Neukom: Speak up now so Mr. Stick can hear you.

A. The connective fat tissue is separated from the glands, and then it is extracted with petroleum ether to get rid of all fatty matter, and then it is dessicated at about 60 to 60 degrees Centigrade, and then it is later powdered up in [77] this thyroid powder of commerce.

The Court: But the ingredient we get is iodine, is it?

The Witness: Is the iodine.

The Court: The rest of it is just a carrier for the iodine, is that it?

The Witness: That is right, sir.

Q. By Mr. Neukom: You conducted tests that you understand, the approved tests, for endeavoring to determine whether there was any thyroid substance present, did you? A. Yes, sir.

(Testimony of Andrew G. Buell)

Q. I observe on the label here that it says "Thyroid Substance 1 grain" or "1 gr." Is that "grain"?

A. That is one grain; yes, sir.

* * * * *

Q. Would you look at 4 so we can have an interpretation of what that one grain means according to the label?

A. The label states that "each cc contains Thyroid Substance 1 grain."

The Court: Does that mean contains one grain of iodine?

The Witness: One grain of the active constituent of [78] the thyroid.

The Court: That is iodine?

The Witness: As organically combined iodine.

Q. By Mr. Neukom: In your opinion, or what did your test reveal, in your opinion, as the amount of thyroid substance in this product, Government's Exhibit 3, when you analyzed it in March of 1946?

A. There was no thyroid present at all.

Q. Is thyroid substance a stable product?

A. Yes; it is, sir.

Q. Is it susceptible to early deterioration?

A. It is considered a quite stable product. Even though it was decomposed, I would still have found iodine in the solution because there was no way for the iodine to escape.

Q. Does extreme heat affect the iodine?

The Court: By that, do you mean does it dissipate it?

(Testimony of Andrew G. Buell)

Mr. Neukom: Yes; dissipate it?

A. No; it could not possibly dissipate it, because the bottle was a sealed bottle, and even though it was decomposed, that iodine would have still been in the bottle.

Q. Even had it all evaporated, would there still have been a crystal form remaining?

A. Yes, sir; it would have still been in there.

Q. In your opinion, would the retention of the product [79] in temperature of an ordinary refrigerator, would that dissipate the thyroid substance?

A. No, sir.

Q. Would the normal temperatures rising even up to 120 or more, would that dissipate it?

A. No, sir.

Q. Assuming this product had been handled—we will assume taking in conjunction—although I know this question is not entirely proper. You heard the testimony of Mr. Mason, did you not?

A. I did, sir.

Q. And assuming that this product here, nothing was added to it, nothing taken from it excepting the amount that chemist Mason took from it; assuming that it was transmitted to you by mail, and the assumption of the findings that you gathered from your tests, have you an opinion as to whether or not this product contained in Government's No. 3 contained any thyroid substance on September 17, 1945?

A. It could possibly have contained no thyroid when it was manufactured.

Q. Assuming the product that you looked at, your opinion back is that it contained no thyroid substance?

A. Yes, sir.

The Court: Would iodine evaporate in any way?

(Testimony of Andrew G. Buell)

The Witness: No. It is organically combined, so that [80] even though the water was evaporated off, the thyroxine and the di-iodo-tyrosine would still be present.

The Court: Suppose you took the contents of this Exhibit 3, and assuming it contained one grain of thyroid substance per each cubic centimeter, and suppose you boiled it, would the iodine or the thyroid substance be dissipated?

The Witness: No; it would still be left. It would still be left and not evaporated off. The water—

The Court: If you boiled it dry?

The Witness: If you would boil it dry, it would still be there.

* * * * *

Cross Examination

By Mr. Stick:

Q. Mr. Buell, I believe you stated that you used an Elmslee-Caldwell method of test? A. Yes, sir.

Q. For the iodine? [81] A. Yes, sir.

Q. What is that test? How do you perform it?

A. Well, I took the 15 cubic centimeters of solution and put it in a nickel crucible and added 10 cc of alcohol, five grams of sodium carbonate, and five cc of 40 per cent sodium hydrochloric acid, evaporated that down to dryness and put it into a muffle furnace.

Mr. Stick: Into a what?

A. Into a muffle furnace at 550 degrees for one-half hour. And then the extract is—then it is taken out of the muffle, cooled down, and boiling water added to it and filtered, and the melt is extracted until all the iodine present is gone through the filter paper into the

(Testimony of Andrew G. Buell)

flask below. That is made up to 300 cubic centimeters and then phosphoric acid is added to it and bromine is then added, and the iodine, any iodine present, is oxidized to the iodate stage, then the excess bromine that is added is entirely boiled off and the product cooled down and potassium iodide is added and titrated off with sodium sulphate standard solution, and from the number of cubic centimeters of thiosulphate solution the amount of iodine is calculated. That is the sum and substance of the test.

Q. By Mr. Stick: Thyroid is a gland in the body of a living animal, is it not? A. Yes, sir. [82]

Q. And this gland contains certain compounds, does it not? A. Yes, sir.

Q. One of those compounds or substances is iodine, or is an iodine compound?

A. It is organically combined iodine; yes, sir.

Q. Combined with what?

A. Well, it is combined as the di-iodo-tyrosine and also as thyroxine.

Q. Now, thyroxine is then one of the substances in the thyroid gland? A. That is right.

Q. Now, what other substances besides iodine or thyroxine are in the thyroid glands?

A. There is no therapeutically active ingredients other than the iodine-thyroxine compounds.

* * * * *

Mr. Stick: I am not asking for "therapeutically active" or anything else. What other substances are there?

(Testimony of Andrew G. Buell)

A. Well, muscle tissue would be one of them, probably a little fat that would be undissolved by the petroleum ether in the preparation of the glands. [83]

Q. Would there be any salts of any kind present?

A. Yes; there would be some sodium chloride present.

Q. Anything else?

A. That is about all I would know.

Q. Would there be any proteins?

A. Yes; there would be proteins present.

Q. Fats? A. Probably a small amount of fats.

Q. Would there be any adrenalin present?

A. I don't know.

Q. You don't know. There would be in a thyroid gland, then, things other than iodine or thyroxine or this other substance that you mentioned similar to it, would there not?

A. There would be other things present,

* * * * *

Q. In your handling of the substance which you took [84] from the bottle, which I believe is Exhibit 3, did you examine what base the contents of that bottle were dissolved in or were held in?

A. No; I did not.

Q. Was it an oil base?

A. I don't think it was oil. It looks like a water solution.

Q. Well, a water base. Is iodine soluble in water?

A. Iodine is, but the organically combined iodine and thyroid is insoluble in water.

Q. Thyroxine is insoluble?

A. Is insoluble in water.

(Testimony of Andrew G. Buell)

Q. What was the name of the other?

A. Di-iodo-tyrosine is the other iodine compound.

Q. And is that soluble in water?

A. That is insoluble.

Q. Then, if this was a water base, you would not expect to find any of those parts of the thyroid gland in the substance?

A. There would be none; no, sir.

Q. There would be none. There could, however, be other parts of the thyroid gland solution?

A. That is possible.

Q. Did you examine the label that was on the bottle, Exhibit 3? [85]

A. Well, when I received the sample the label had been removed for the records. I have since seen the label, though.

Q. Did you see the label at the time that you made your examination?

A. Yes. I received the records and the label was included in the records.

Q. In the records? A. Yes, sir.

Q. I have here Exhibit No. 4, which is a sheet of paper on which there appears a label. Is that the label that you saw at the time that you made this examination and test? A. Yes; it is.

Q. Did you read that label?

A. Yes. That is one of our duties, is to read the label before we start the analysis.

Q. Did you read on there this portion: "This preparation does not contain any known therapeutically useful constituent."? A. I read that, sir.

(Testimony of Andrew G. Buell)

Q. Did that indicate to you that there was no active substance of thyroid in that solution?

A. Well, you would draw that conclusion from reading that; but I did not let that influence me at all when I made my analysis. [86]

Q. So you examined for iodine? A. Yes, sir.

Q. And only for iodine? A. That is right.

Q. And for no other thyroid substance than iodine?

A. That is right.

Mr. Stick: That is all.

Redirect Examination

By Mr. Neukom:

Q. Mr. Buell, did you find anything in this product which you can identify as a thyroid substance?

Mr. Stick: He just said he made no examination in regard to it.

A. The only thing I examined it for was for the therapeutically active ingredients of thyroid, which were the organically combined iodine products.

Q. What do you mean by the "therapeutically active"?

A. Well, the therapeutically active constituent of thyroid is thyroxine and the di-iodo-tyrosine.

Q. Those you did not find?

A. And they weren't present.

The Court: They were not present?

The Witness: They were not present, your Honor.

Q. By Mr. Neukom: Do you know of any other test, [87] either as denominated in the Pharmacopoeia

(Testimony of Andrew G. Buell)

or from your own experience or knowledge, of detecting a thyroid substance other than the one you have related?

A. No; that is the only test that we use, is the one used in the Pharmacopoeia, which is almost identical with the method I used.

Q. Is that the accepted test among chemists and analysts of good repute?

A. Yes; that is a test that all chemists used for a detection of thyroid, is the organically combined iodine method.

Mr. Neukom: That is all. Did you want some questions?

The Court: No; I have nothing further.

Mr. Neukom: Mr. Capps. We have but two more witnesses, your Honor, on the case in chief.

HUBERT H. CAPPS,

called as a witness by plaintiff, being first sworn, was examined and testified as follows:

The Clerk: Please state your name.

The Witness: Hubert M. Capps.

Mr. Neukom: We are now taking up Counts III and IV, your Honor, what is known as the Pluri-B. [88]

Direct Examination

By Mr. Neukom:

Q. Did you have occasion to analyze a substance known as Pluri-B? A. Yes.

Q. And about what date did you conduct your analysis?

* * * * *

(Testimony of Hubert H. Capps)

The Witness: It was in September, 1945, the 24th, I believe.

* * * * *

Q. What is your business or occupation, that is to say, as of the date that you just testified to, September, 1945?

A. I was a chemist for the Food and Drug Administration.

Q. And working in Washington, D. C.?

A. That is right. ,

Q. And assigned to what division?

A. The Vitamin Division.

Q. And had been so employed for about how long prior to that?

A. About six years in the Vitamin Division.

Q. What was your education or background along your [89] specialty line?

A. I have an A.B. from Hardin-Simmons University in Texas.

Mr. Neukom: Speak up so we can all hear you.

A. And I have a master's degree from the University of Washington in Seattle; and I did some graduate work in Iowa State College.

Q. In the chemistry field?

A. Yes; all of it was in chemistry.

Q. And did you have any other experience along that line after graduating, other than that that which you had with the Food and Drug Administration?

A. Well, I taught chemistry up until the time I came with the Food and Drug Administration.

* * * * *

(Testimony of Hubert H. Capps)

Q. By Mr. Neukom: And while you were with the Food and Drug Administration did you have occasion to analyze various products? A. Many of them.

Q. And particularly in conjunction with ascertaining whether or not products had the substances we commonly refer to as B-1 and B-2? [90]

A. Well, B-1 and C, chiefly; B-1 and Vitamin C.

Q. I see. Incidentally, what is the correct chemical or chemical term for the B vitamin?

A. B-1 is ordinarily called "thiamine" or "thiamine hydrochloride".

Q. And what is "riboflavin"?

A. That is ordinarily called Vitamin B-2. Both of them as B-complex.

Mr. Neukom: Now, I am going to have marked for identification a vial as Government's next in order.

The Clerk: 6 for identification.

Mr. Neukom: And a label on a sheet of paper.

The Clerk: 7 for identification.

Q. By Mr. Neukom: In the course of your duties with the Food and Drug as a chemist, did you have occasion to receive a vial containing a product such as reflected by Government's Exhibit 6 for identification? Did you have occasion to receive that? A. Yes.

Q. And did you conduct an analysis of the contents of that? A. I examined it for thiamine.

* * * * *

Q. And just explain what you did. [91]

A. Well, I followed the procedure described in the U. S. Pharmacopoeia, with modifications for this type of product.

(Testimony of Hubert H. Capps)

Q. Speak up louder.

A. The Thiachrome procedure for thiamine described in U. S. P.

Q. Did you have before you Government's Exhibit 7, the label of this product Pluri-B, in conducting your examination?

The Court: Did you have the label or had you seen the label?

The Witness: The label was attached to this bottle, I believe.

The Court: The witness refers to Exhibit 6 for identification.

* * * * *

A. Exhibit 6 and Exhibit 7. Exhibit 6, at the time I examined the sample, was on the bottle or attached.

* * * * *

Q. By Mr. Neukom: Is there anything on this label now of your markings?

A. Yes. I have my initials on the label.

Q. Indicating the black ink?

A. The date of examination and my initials. [92]

Q. "9-24-45 H. H. C.", is that correct?

A. That is correct.

Q. You will observe that the label says "Thiamine Hydrochloride—50 Mgms."—milligrams that is, isn't it?

A. Yes.

Q. And above that it says: "Each cc contains," and then the list of the various products, is that correct?

A. That is right.

(Testimony of Hubert H. Capps)

Q. Now, you conducted a test of this product which came to you, and in doing so did you ascertain whether or not each cc did contain 50 milligrams of thiamine hydrochloride?

A. My examination showed that this product, at the time I examined it, contained 33 milligrams per cubic centimeter, approximated.

* * * * *

Q. 33 instead of 50? A. That is right.

Q. Is thiamine hydrochloride, excepting when exposed to extreme high temperatures, is it reasonably a stable product?

A. In a properly made solution it is stable.

Q. Did you note whether or not this solution, in your examination, was in an oil base or a water base or what type of base? [93]

A. It was possible to mix it up with water and it dissolved completely in water, the solution did, so it was in a solution that is miscible with water. Presumably it was water.

Q. It was not then in an oil base?

A. It was not an oil.

Q. You examined the product in September, is that correct. A. 9-24-45.

* * * * *

Q. Now, assuming that the product received ordinary and reasonable care, and was not exposed to excessive heats, such as heats any more than would be normal from shipping and the weather, and basing upon what you found on September 24, 1945, the amount of the

(Testimony of Hubert H. Capps)

B-1 or thiamine chloride that you found, have you an opinion as to what percentage or what amount that product, substance, or solution had on or about July 16, 1945, the date it was originally shipped?

A. I believe it did not contain as much as 50 milligrams; not more than 33.

Q. Your opinion is then it contained about 33?

A. 33 milligrams per cubic centimeter.

Mr. Neukom: That is all. Counsel may cross examine. [94]

Cross Examination

By Mr. Stick:

Q. Where did you conduct this examination?

A. In my laboratory in Washington.

Q. Day time or night time?

A. Well, in the day time.

Q. Is there a name to the test that you used, like there have been to some of these others?

A. We ordinarily call it the Thiachrome procedure.

* * * * *

Q. What do you mean by a Thiachrome procedure?
What is the procedure?

A. Do you want me to go into detail in it?

Q. Yes; I do. A. Complete detail?

Q. Thiachrome—"chrome" has to do with color, doesn't it? A. Well, yes, usually.

Q. And this procedure is a procedure that is carried out by the matching of colors; is that true?

A. No; it is not. The thiamine in the solution is converted into a material called thiachrome. This material

(Testimony of Hubert H. Capps)

flouresces and the fluorescence is measured, and from the amount of fluorescence we know the amount of thiamine that [95] was present in the beginning.

Q. And how is this fluorescence measured?

A. We have a flourometer for measuring it. It is an electrical instrument.

Q. Does it measure or is it measured by a comparison of colors between the substance and a known standard?

A. We have a standard thiamine solution and we measure the amount of fluorescence from that standard thiamine solution; and we also have a solution of this material that we are examining and we measure the fluorescence from that material, and we compare the fluorescence of the two and get our results.

Q. Now, just what do you mean by "fluorescence"?

A. With a material that will fluoresce, if a light of shorter wave length is passed through a solution, for instance, a thiachrome, a light of a longer wave length will be emitted, and we measure that light that is emitted.

Q. What is the accuracy of tolerance in that test?

A. The test with a solution like this would give us about five per cent, not more than five per cent difference.

The Court: Do you use the same quantity of the solution for the standard as you do for the material under examination, the substance under examination?

The Witness: We dilute them up so that the standard will have the same quantity of thiamine to begin with as our [96] sample. Both of them are diluted up in order to get the same amount of thiamine. We have to dilute them in the same way. Now, when the—

(Testimony of Hubert H. Capps)

The Court: What you are searching for is the amount of thiamine, isn't it?

The Witness: That is right.

The Court: What do you mean by "we dilute them up until we get the same amount of thiamine"?

The Witness: Our standard solution contains one milligram or one microgram of thiamine per cubic centimeter.

* * * * *

Mr. Stick: What is this you have in your hand?

A. These are my notes that I made at the time of the examination.

Mr. Stick: All right.

A. The standard solution was diluted up so that it [97] contained one microgram of thiamine per cubic centimeter. The Pluri-B was diluted also so that it would contain one microgram of thiamine per cubic centimeter, assuming that it contained 50 milligrams of thiamine originally.

The Court: As stated on the label?

The Witness: As stated on the label. Then when the thiamine was converted into thiachrome—

Q. By Mr. Stick: In each instance?

A. In each instance, both in the standard and in the sample, the readings were made for the fluorescence, and it was less for the sample than it was for the standard solution.

The Court: Presumably they would be the same?

The Witness: Presumably they would be the same if the sample originally contained 50 milligrams of thiamine per cubic centimeter.

(Testimony of Hubert H. Capps)

The Court: Were both solutions in the same type of container?

The Witness: They were treated as nearly as possible exactly the same.

* * * * *

Q. By Mr. Stick: At the time you took the solution which is in the bottle before you, Exhibit 6, and diluted [98] it, there were in that dilution also other substances, were there not?

A. The label states that the product contains riboflavin, pyridoxine hydrochloride, pantothenic acid, and nicotinamide.

Q. And they were in the solution that you diluted?

A. Necessarily.

Q. Did you make any test for riboflavin?

A. No.

Q. For pyridoxine hydrochloride? A. No.

Q. Pantothenic acid did you test for?

* * * * *

A. No.

* * * * *

Q. Nicotinamide. Did you make any test for that?

A. No test.

The Court: You had thiamine hydrochloride. Say this solution that you were examining, Pluri-B, contained other ingredients and other properties, did you make an allowance for those?

The Witness: Do you mean, for instance, the riboflavin, pyridoxine chloride, pantothenic acid and nicotinamide? [99]

(Testimony of Hubert H. Capps)

The Court: Yes. Was your standard solution comprised of the diluting solution and the thiamine hydrochloride alone?

The Witness: Yes; the standard is.

The Court: Then your solution under examination is composed of thiamine hydrochloride and your diluting solution, plus these other items that are mentioned on the label which is Exhibit 7 for identification before you there?

The Witness: That is right.

The Court: In making the test do you make any allowance for the fact that the solution under investigation contains other properties than the standard solution contains?

The Witness: During my time with the Food and Drug Administration I examined probably 2,000 samples that some of them had the other ingredients present, for instance, riboflavin, nicotinamic acid, pyridoxine, and things of that kind, and I never could find any difference. It didn't make any difference whether they were present or whether they were not present as far as the thiamine was concerned.

The Court: This fluorescence test, is it based upon a reflection of light that the presence of thiamine hydrochloride will make or cause?

The Witness: Yes. The light, the fluorescent light, is generated, you might say, by the light that falls on the solution of thiamine. [100]

* * * * *

The Court: Will the presence of riboflavin change that color?

(Testimony of Hubert H. Capps)

The Witness: In the solution that we actually measure, the solution or thiachrome that we actually measure, there would not be any riboflavin present.

The Court: Well, I mention that only by way of example. Assume the presence of all or any of the other materials that are mentioned on the label, Exhibit 7 for identification.

The Witness: I will go a little more into detail in the procedure. These solutions are made up, and then after the conversion into thiachrome and before the measurement is made, the thiachrome is extracted with an isobutyl alcohol, and the other items, pyridoxine, riboflavin and nicotinamic acid would be left behind in the water solution.

The Court: So when it comes to the actual test of the two solutions, the standard solution and the solution under investigation have the same chemical properties, is that correct?

The Witness: As nearly as possible.

The Court: I mean quality, not quantity?

The Witness: That is right.

The Court: That is all I have.

Q. By Mr. Stick: At the time you received the vial or [101] bottle, Exhibit No. 6, did it have the cap on that it has now?

A. It did, or one very similar to it; and since this does not appear to be broken, I think that it did have that identical cap.

Q. And did you make any examination of that cap to determine whether or not it was punctured in any way, other than just looking at it?

A. No.

Mr. Stick: That is all.

Mr. Neukom: That is all. May I offer in evidence the vial, if I have not already? I don't think I have. 6 and 7, may I offer into evidence, your Honor?

The Court: Exhibits 6 and 7 for identification are received into evidence. [102]

[GOVERNMENT'S EXHIBIT NO. 7]

30 cc STERILE SOLUTION No. 256
PLURI-B

(Some factors of the B Complex)

For Intramuscular Use

EACH CC CONTAINS:

Thiamine Hydrochloride	50 Mgms.
Riboflavin	1 Mgm.
Pyridoxine Hydrochloride	10 Mgms.
Pantothenic Acid	10 Mgms.
Nicotinamide	50 Mgms.
Chlorobutanol (Chloroform deriv.)	1/12 gr.—0.005 Gm.

CAUTION: To be used only by or on the
prescription of a physician.

PASADENA RESEARCH LABORATORIES, Inc.

Pasadena 8, Calif., U. S. A.

Lot No.

[Written]: 29953 H. 8-30-45 F.A.G. 9-14-45 ONK
9-14-45 HWF 9-24-45 HHC

Case No. 19223. U. S. vs. Pasadena Laboratories. U. S. Exhibit 7. Date 6/18/47. No. 7 in Evidence. Clerk, U. S. District Court, Sou. Dist. of Calif. L. J. Somers, Deputy Clerk.

No. 11690. United States Circuit Court of Appeals for the Ninth Circuit. Filed Aug. 25, 1947. Paul P. O'Brien, Clerk.

* * * * *

DEFENDANT'S CASE IN CHIEF

RUSSELL R. BAVOuset,

a defendant herein, called as a witness by defendants, being first sworn, was examined and testified as follows: [121]

The Clerk: Please state your name.

The Witness: Russell R. Bavouset.

* * * * *

Direct Examination

By Mr. Stick:

Q. What is your occupation, Mr. Bavouset?

A. I am general manager of the Pasadena Research Laboratories.

Q. How long have you been with that organization?

A. This is the sixth year.

Q. What are your duties there, generally?

A. Overseeing the production of materials.

Q. The production is made under your direction?

A. Yes, sir.

Q. What is your education and experience with reference to the manufacture of—what do you call it, biological preparations? [122]

A. Yes, sir. Well, this is my 20th consecutive year in the business. I have studied general chemistry and organic chemistry. I had some work in technology, etc., but most of my work has been practical, under Dr. E. S. Miller for 13 years, Dr. Simonson, etc., those people that I have worked with.

Q. In that time you have been in the work of manufacturing various preparations such as the ones that are referred to herein?

A. Yes, sir.

(Testimony of Russell R. Bavouset)

Q. How long have you been making these preparations that are referred to in the information?

A. I believe the Vitamin B-1 products have been in existence now something like 10 years. I have been making solutions of Vitamin B-1 and B-complex solutions 10 years.

Q. And Vitamin D?

A. Vitamin D (in oil) is a relatively new product, that is, the injectable Vitamin D (in oil); and I believe the first we made of that was late in 1945.

Q. And the Indoform?

A. Indoform is an aqueous extract. We have been making that—I have been making that over a period of about 15 years.

Q. By “aqueous extract” what do you mean with reference to Indoform? [123]

A. Aqueous extracts are generally made with either raw glands or dessicated glands, and they are extracted with water under septic conditions, and after a period of time they are processed to eliminate unfavorable materials, and bottled and sterilized and put on the market.

Q. I will show you Government's Exhibits 3 and 4, 3 being a vial and 4 being the label taken from that vial, the labial vial called “Indoform.” It has been alleged here that that was shipped from your laboratory on September 17, 1945. Is this matter manufactured in quantities of single vials or in quantities of a number of vials?

A. In quantities of a number of vials.

Q. And who manufactured the particular product that was contained in the bottle before you? A. I did.

(Testimony of Russell R. Bavouset)

Q. Will you state your procedure in the manufacture of that?

A. In the manufacture of this particular preparation an aqueous—that is water—as the extractive is used and a flask containing whole ovarian, another containing anterior pituitary, and another containing thymus, thyroid, and lymphatic were all extracted separately, after which time they were filtered off and given the usual process of freeing that of foreign proteins and undesirable factors, combined and reduced to amount, and then suprarenal cortex from a concentrate [124] was added, and finally a posterior pituitary, and made up to the required volume containing the preservatives.

Q. And then the substances were placed in vials?

A. That is correct.

Q. And the vials were shipped out to the several parties as referred to in this particular instance, Dr. Joseph C. Buntin in Cheyenne, Wyoming? A. Yes.

Q. And this was one of several that were shipped to him. At the time that that was shipped was there three international units of *poterior* pituitary in a cubic centimeter of the contents of that bottle?

A. Yes. I measured out that amount for this particular solution.

Q. And was there one grain of thyroid substance in that matter at that time?

A. There was aqueously extracted one grain per cc of thyroid.

Q. Would that be the substance that contains iodine?

A. No, sir.

Q. Is the iodine substance of thyroid or thyroxine soluble or extractable in water? A. No, sir.

(Testimony of Russell R. Bavouset)

Q. There are other substances in thyroid than the iodine or thyroxine? [125]

A. There seems to be. Doctors request it.

Q. And you sell this preparation to doctors?

A. We do.

Q. And only to doctors? A. That is correct.

Q. They order it direct from you?

A. They order either direct by mail or through one of our salesmen.

The Court: What do you mean by "thyroid substance"?

The Witness: You take the powdered thyroid, that is the dessicated thyroid, and put it into a flask containing water, a measured amount of water, and that is extracted by shaking it over a period of time, usually two weeks. That is not continuously shaken, but several times a day, shaken up thoroughly and allowed to stand and then filtered off, and that material which is soluble in the water is then put into vials, with due process of sterilization, etc.

The Court: Then this Indoform did not purport to contain any iodine?

The Witness: No, sir.

The Court: What is the thyroid substance here it did purport to contain?

The Witness: Your Honor, I do not know the type of material that is designated therein. We put a disclaimer on that product, stating that it did not contain therapeutically [126] useful constituents, to definitely let the doctor know that the thyroid content was not the iodine content.

(Testimony of Russell R. Bavouset)

The Court: In the trade would the term "thyroid substance" have any particular meaning?

The Witness: In the trade the words "thyroid substance" for oral administration would mean the whole gland, that is, of course, meant to feed it or made ready for oral administration.

The Court: And that would contain iodine?

The Witness: Yes, your Honor; that would contain iodine.

Q. By Mr. Stick: In an aqueous solution would it contain that? A. No, it would not.

The Court: Is there anything on this label, this Indoform label, to indicate it is an aqueous solution?

The Witness: I do not believe so, your Honor. I believe we merely take that for granted, that it is an injectable, sterile injectable, and by its physical appearance is of aqueous nature.

The Court: Are there any words or symbols on the label which would tell a physician that this was an aqueous solution?

The Witness: I do not believe so, your Honor. The words "30 cc" would state that it was a solution, but not necessarily aqueous.

The Court: Of course, the fact it was liquid would indi- [127] cate a solution, too.

The Witness: Yes, sir. I believe, other than that, there is no indication.

Q. By Mr. Stick: Is thyroid substance in the form of thyroxine administered by injection?

A. I am not acquainted with any such preparations. There may be.

(Testimony of Russell R. Bavouset)

Q. Is the water-soluble extract administered by injection?

A. Yes; the water-soluble extract is administered by injection.

Q. I will show you the next combination of exhibits 6 and 7 of the Government.

The Court: Before you leave this thyroid question, I would like to ask the witness: Is there any other article on the market that you know anything about that has a label which specifies "thyroid substance" that does not contain any iodine?

The Witness: Yes, your Honor; there are many such preparations similar to this one and with thyroid, alone; that is, there is thyroid substance by itself without other materials in with it. There are many such preparations on the market, used daily.

The Court: That contain no iodine?

The Witness: Yes, your Honor. [128]

The Court: Sold to physicians?

The Witness: Yes, your Honor.

Q. By Mr. Stick: Do you have any of those substances? A. Yes; we do.

Q. Here?

A. I do not believe I brought anything like that along. I do not think I have a vial of thyroid substance here.

Q. Just plain thyroid substance?

A. Yes. I do not believe I have anything like that here.

Mr. Stick: If this matter goes over until tomorrow, will he be permitted to bring some of it in to show your Honor, and may I recall him at that time for that purpose?

(Testimony of Russell R. Bavouset)

The Court: Yes. He stated there are such. Unless the Government wishes to rebut it, I don't know whether there will be an issue as to that or not.

Mr. Stick: I see. Looking at Exhibits 6 and 7, 6 being a bottle and 7 being the label, that bottle—that is the correct combination, it it not, Mr. Neukom; 6 and 7 together is Count II?

Mr. Neukom: Counts III and IV, isn't it?

Mr. Stick: Or, Counts III and IV; yes.

Q. That label bears the mark "PLURI-B." That material was manufactured at your plant?

A. Yes; it was. [129]

Q. And by whom?

A. Probably by myself or—may I have that date?

Q. That was shipped 7-16-45, July 16, 1945.

A. It was probably made by myself.

Q. Made by whom?

* * * * *

Q. And will you state how that was made?

A. Those vitamins there are all aqueous soluble, that is, water soluble, and a combination is usually weighed out; that is, first, we weigh the thiamine chloride, Pyridoxine hydrochloride, and the calcium pantothenate in separate containers. The calcium pantothenate is converted into pantothenic acid, then the thiamine and pyridoxine and pantothenic acid are combined in one solution; then the riboflavin and the nicotinamide are combined in another solution, and it takes heat to put the riboflavin in. The nicotinamide is instrumental in putting riboflavin in solution. It is many times more soluble with nicotinamide present. So they are combined together and heated until

(Testimony of Russell R. Bavouset)

dissolved, after which time the pH. is adjusted to meet the pH. of thiamine and pyridoxine, approximately a pH. of 3.2. Then they are added together and processed with a glandular substance added in. A process for the purpose of eliminating any foreign material that might come down is gone through, chiefly bringing to boiling for 10 minutes and ice boxing for 48 hours. [130]

Q. Thus all of the matters set forth in the label there are combined into that solution? A. Yes, sir.

Q. And that, too, is mixed in amounts larger than that of a single vial? A. That is correct.

Q. And then the matter is put into these vials under 30 cubic centimeters to the vial?

A. That is correct.

Q. And at the time that solution is bottled does it have the full strength and potency that is set forth on the label? A. It does.

The Court: Have you had considerable experience in dealing with thiamine hydrochloride?

The Witness: Yes, your Honor; about 10 years.

The Court: Does it deteriorate in the bottle?

The Witness: Well, under certain conditions it does, your Honor.

The Court: What are those conditions supposed to be?

The Witness: Well, there are conditions such as where the pH. is not correctly adjusted, where the glass is not properly prepared ahead of time, that is, the vial that it is put in is not properly prepared ahead of time. There are deteriorating factors such as foreign particles that might be [131] introduced into the vial. There are deteriorating factors such as light and heat, exposed to air over a period of time.

(Testimony of Russell R. Bavouset)

The Court: But if this solution containing a certain quantity of thiamine hydrochloride is put in one of your bottles and sealed, is there any reason why, if it were examined six months later, it would contain any less than you put into it?

The Witness: I am not personally too familiar with that particular aspect. I could not say definitely one way or another.

The Court: What would be the situation with respect to posterior pituitary?

The Witness: There are certain factors that could cause that to deteriorate.

The Court: What would those be?

The Witness: Well, I would prefer to allow our gentleman who takes care of that explain it, as I am not as familiar with that as he is. [132]

* * * * *

Q. To go back a moment, again, to the Exhibits 6 and 7, the Pluri-B, I will ask you at the time that was made was [133] there an override of any of the material used in the manufacture of that?

A. I believe at that time we were using about five per cent override.

Q. Of what? A. Thiamine hydrochloride.

Q. Why?

A. Thiamine hydrochloride, in processing, has a very definite tendency to become impotent; it breaks down. It is a product that has certain deteriorating factors in it, and when handled it does break down. There are two types or possibilities of break down of that particular material. One will break down in heat, the other will break down in cold; and thus, as the break downs are

(Testimony of Russell R. Bavouset)

natural, to the detriment of thiamine chloride and natural to the Vitamin B product itself.

Q. And for that reason you put in this override?

A. That is correct.

The Court: Do you know of any danger of putting too much thiamine hydrochloride in that product?

The Witness: No, your Honor. There is very, very little toxic effect of thiamine hydrochloride in four times and up that particular strength.

Q. By Mr. Stick: The fact is that these vitamins are foods, are they not? [134]

A. That is correct.

Q. Vitamin B-1 is found in the foods that we eat normally, is it not?

A. That is right.

Q. Now, I show you Government's Exhibits Nos. 1 and 2, I believe they are.

Mr. Neukom: Those are the ones you have there. Do you want the label?

Q. By Mr. Stick: The one being two bottles in a box, and two being labels from those bottles; and they are marked "Pluri-B." Were these manufactured in your plant?

A. Yes; I understand they were.

Q. How were they manufactured and under whose supervision?

A. Under my own.

Q. These products are part of a shipment that is in evidence as having been made on June 18, 1946, to Dr. Ryerson in Phoenix, Arizona. It was part of a shipment?

A. That is right.

Q. Do you recall how much the original shipment was?

A. I believe the original shipment was about 50 vials.

(Testimony of Russell R. Bavouset)

Q. Will you state how that product was made? By the way, is that the same product as the other Pluri-B that we have here?

A. It is the same product, with one exception. Ribo- [135] flavin has been increased to two milligrams, instead of one milligram as the previous product.

Q. This product here has two milligrams of ribo-flavin? A. That is right.

Q. And the one in Exhibits 6 and 7 has one milligram? A. That is right.

Q. And other than that they are manufactured in the same way and contain the same ingredients?

A. That is correct.

Q. And were manufactured in lots larger than the one bottle or two bottles, and then were bottled and shipped? A. That is right.

Q. In the 30 cc vials? A. Yes, sir.

Q. I will ask you to look at the two bottles in Exhibit 1, look through them. Do you see anything in those bottles other than the liquid solution?

A. Yes; there is a precipitate.

Q. Was that precipitate in those bottles at the time you made it? A. No; it was not.

Q. Or when you finished making it?

A. No; it was not.

Q. Was that precipitate in those bottles when you shipped it to Dr. Ryerson on June 18, 1946? [136]

A. No; it was not.

(Testimony of Russell R. Bavouset)

Q. Before any of these materials are shipped have you any means in your office of checking these products?

A. We keep control batches for a short time after the material has gone out of the business, or the place of business.

Q. Are there any inspections made at the time they are shipped out?

A. Yes; a very careful inspection is made the last thing before it is placed in shipping cartons and sent out and marketed.

Q. By whom is that inspection conducted?

A. Well, we have one young lady at the head of the stock department, Mrs. Evelyn Smiley. There is another young lady, one of two assistants, that would likewise inspect this material before it goes out.

Q. And who is this young lady in charge of the shipping department?

A. Evelyn Smiley.

Q. And she is here?

A. She is. [137]

* * * * *

Mr. Stick: If it please the court, I have a young lady from the laboratory here whose testimony will take but a few minutes. It is agreeable to counsel for the plaintiff that I may call her out of order, if your Honor has no objection.

The Court: No. You may call her. Had you completed the direct examination of Mr. Bavouset?

Mr. Stick: No, I had not.

(Witness withdrawn.)

EVELYN M. SMILEY,

called as a witness by defendants, being first sworn, was examined and testified as follows:

The Clerk: Please state your name.

The Witness: Evelyn M. Smiley.

Direct Examination

By Mr. Stick:

Q. Mrs. Smiley, what is your occupation?

A. I am head of the shipping department.

Q. Where?

A. At the Pasadena Research Laboratories. [138]

Q. How long have you been with the Pasadena Research Laboratories?

A. It will be three and one-half years very shortly.

Q. You went with them in the year 1944?

A. That is right.

Q. And have been with them ever since?

A. Yes.

Q. How long have you been in charge of the shipping department?

A. About three years.

Q. Were you in charge of the shipping department on the 18th of June, 1946?

A. Yes; I was.

Q. And you were there at the laboratory at that time?

A. Yes, sir.

Q. What are your duties there?

A. Well, I received the invoices and the sale order and a shipping label from the office and clip those together with the packing slip. Then I go to the stock shelves and fill the invoice from the stock shelves. Then I take the orders, put my initials on the packing slips, check the vials, the solution in the vials, to be sure there is no foreign particles, before I put it on the invoice

(Testimony of Evelyn M. Smiley)

on the other table for the next girl to package and box and ship out.

Q. Now, the next girl who boxes for shipping, is she [139] under your direction? A. Yes; she is.

Q. Do you supervise her work? A. Yes.

Q. She puts the same boxes in the shipping package that you have selected and have examined? A. Yes.

Q. And then after they are put in the shipping package they are sent by parcel post? A. Yes, sir.

Q. And who sends them by that? A. I do.

Q. I will show you Plaintiff's Exhibits 1 and 2, 1 being two bottles of a substance called "Pluri-B", 2 being the labels from those bottles. I state to you that they were, by the evidence, shipped to Dr. Ryerson in Phoenix, Arizona, on June 18, 1946. Those bottles went through your selection and packing? A. Yes, sir.

Q. I will ask you to examine those bottles and state if you see anything in the contents of them other than this liquid?

A. Yes; I do. There are foreign particles.

Q. Were those foreign particles in there at the time that you selected them and tagged them? [140]

A. They were not.

Q. You examined for that purpose? A. Yes.

Q. You examined all of them for that purpose?

A. Yes.

Q. How long after you pack them is it that you send them by mail?

A. Usually I start packing about 8:30 in the morning and we take the packages to the post office about 4:30 at night.

(Testimony of Evelyn M. Smiley)

Q. So that they are mailed that day, the same day they are packed? A. Yes.

Q. Might it occasionally be that they are mailed the next day? A. Very seldom.

Q. Would that be mailed later than the next day, at any time? A. No.

Mr. Stick: Take the witness.

Cross Examination ,

By Mr. Neukom:

Q. What is your name, again? I didn't get that.

A. Evelyn Smiley. [141]

Q. Mrs. Smiley. Mrs. Smiley, you have a distinct recollection of having examined 50 bottles on June 18, 1946. Is that just because it is generally your habit to look at the bottles?

A. Well, I very seldom have an order that large. I think I could say that I remember the order.

Q. Well, you think you can say. Do you definitely recall this particular shipment?

A. No; I would not say definitely.

Q. You make a great many shipments, do you not, of vials of like size and all? A. Yes.

Q. Mrs. Smiley, for what reason did you examine to see if the particles were in there? You have been with this concern about three and one-half years, have you not? A. Yes.

Q. And haven't you found that, or have you found that, in most instances the sterile solutions were free of particles such as you note here? A. That is right.

Q. Then it would be rather unusual to find them; would that be it? A. Yes.

(Testimony of Evelyn M. Smiley)

Q. But you had found them in the past?

A. Occasionally; yes. [142]

Q. And that is the reason why you think you recall looking on this date here?

A. No. It is just force of habit, I would say. I always look at them. I never box anything unless I do look at it.

Q. What do you do; do you put them up to some light that you have there? How do you go about that?

A. We have an inspecting lamp, and then we have a light over the table that I package on. I always hold it up to the light before I select and put it in the box.

Q. Your best recollection, that you are definite on it, is that none of the 50 had any particles in them when you shipped them? A. No, sir.

Q. But you have seen particles in other batches of similar material there at the plant; is that true?

A. I have found some.

Q. What have you done about that?

A. We always take it back upstairs.

Q. Have you ever told Mr. Bavouset about finding undissolved particles in sterile solutions?

A. Yes, sir.

Q. When do you recall having told him that?

A. Oh, I would say about two weeks ago.

Q. And was that also in a sterile solution? [143]

A. Yes.

Q. And have you found undissolved particles in any of the other products that were sold for intravenous or intramuscular injections? A. Very few.

(Testimony of Evelyn M. Smiley)

Q. Is there a chemist there or a pharmacist that you have also talked to about finding such a thing, such a foreign particle?

A. I always spoke to Mr. Bavouset about it.

Q. Mr. Bavouset really sort of controls the whole concern, is that correct? A. Yes.

Q. He hires you and was in charge of your duties?

A. Yes.

Q. Is that right? A. Yes.

Mr. Neukom: I think that is all.

Redirect Examination

By Mr. Stick:

Q. Was it your instructions from Mr. Bavouset when you assumed your duties there to make these inspections?

A. Yes.

Q. Invariably? A. Yes. [144]

Mr. Stick: That is all.

Mr. Neukom: Just one question.

Recross Examination

By Mr. Neukom:

Q. They were labeled when you examined, weren't they? A. Yes.

Q. The labels went around about half of the bottles, didn't they?

A. I can always see plainly what is in it, even though the label is on it.

Q. The label such as reflected here on Government's Exhibit No. 2, this label went around the bottle as far as it would go around, is that correct? A. Yes.

Q. And was glued on there? A. Yes.

(Testimony of Evelyn M. Smiley)

Q. And you did not know when these bottles had been manufactured or bottled; you just knew that they were in stock and you went to the stock and procured them and looked at them and had them packed, is that correct? A. Yes. [145]

* * * * * * * *

RUSSELL R. BAVOuset (Recalled)

Direct Examination (Resumed)

By Mr. Stick:

Q. Mr. Bavouset, you have known Mrs. Smiley who was just on the stand preceding you?

A. Yes; I do.

Q. She has been in your laboratory, she said, since 1944; that is correct? A. That is correct.

Q. At the time she took charge of the shipping department what instructions did she have with reference to inspection of materials?

A. Before any of the material may be packed after it is taken off the stock shelf, it is to be inspected very carefully.

Q. You gave her that instruction?

A. I did. [146]

Q. That was an invariable part of your procedure in your laboratory? A. Very definitely.

Q. Is that standard practice in other laboratories where you have worked?

A. Yes; it has always been standard practice.

Q. In the laboratories in which you have worked?

A. In which I have worked; yes.

(Testimony of Russell R. Bavouset)

Q. Have you ever visited other laboratories than those in which you have worked?

A. Well, I have visited several locally, but as to whether that was standard practice there I couldn't say.

Q. Do you know whether they performed or went through with the same practice there?

A. I know that they inspected them very carefully. Whether it was just before they were packed I couldn't say.

Q. That is in those that you were not working in?

A. Yes, sir.

Q. Do the inspectors of the Food and Drug Department come to your laboratory? A. Yes; they do.

Q. And have over what period of time since they first came there, approximately?

A. Oh, I believe the first appeared there very shortly after we started in business, say, five years ago. [147]

Q. Did they make any inspections of the plant?

A. Yes. I believe about once a year they go through the plant very thoroughly.

Q. How often do they come there, in general?

A. Well, sometimes they would come as often as once that month, and sometimes once in three months, sometimes even less frequent.

Q. Did they at any time ask to see your books and shipping records? A. Yes; they do.

Q. What did you reply to them when they asked to see them?

A. Well, my first experience with the Pure Food and Drug inspector was, perhaps, four years ago. I asked one of the gentlemen there about his authority to examine our records and he assured me he had such authority.

(Testimony of Russell R. Bavouset)

Q. Did you ever ask any of the other inspectors that came there, besides him, whether they had any authority to inspect your records?

A. I have spoken to them about their authority, from time to time; yes.

Q. What did they say? [148]

* * * * *

A. They always assured me they had the authority to examine our records.

The Court: What records?

The Witness: Invoices which we file after the regular invoice has been shipped out.

The Court: You mean your office copy of the invoice?

The Witness: Yes, your Honor.

The Court: That is the invoice to the physician and customer?

The Witness: The duplicate invoice to the physician; [151] yes, your Honor.

Q. By Mr. Stick: And those were inspected by the inspectors? A. Yes, regularly.

Mr. Stick: Take the witness.

Cross Examination

By Mr. Neukom:

Q. Mr. Bavouset, none of the inspectors took any products from you that have been offered here in evidence, did they? A. No, sir.

Q. So far as you know, they obtained all of those from people that you had freely and willingly mailed the product to, did they not? A. As far as I know.

(Testimony of Russell R. Bavouset)

Q. And you had no objections to any of your customers turning over to the Food and Drug inspectors any of your product, had you?

A. No; I had no objection.

Q. Your product was open on the market, and if I had walked in there and said I was a doctor and wanted to buy your products, you would have sold them to me, wouldn't you?

A. I would have sold them to any ethical medical doctor. [152]

Q. And if any food and drug inspector had come up and told you he would like to have bought a product, because he wanted to make an analysis of it, you would not have objected at all?

A. I would had it been a product of ours.

Q. Objected to the food and drug officers having your product to make a proper inspection or analysis?

A. They wouldn't have done that, because it is not within the state; so I know that they wouldn't want anything of that kind.

Q. You would have objected to that, though, would you, Mr. Bavouset?

A. Well, I couldn't say. I don't know of any reason why I should have.

Q. All right. Now, your product here, we will take the labels. You were responsible for these labels, were you not?

A. Yes.

Q. For the contents of them?

A. Yes.

Q. And you gave the labels some thought before you had them printed?

A. Yes.

Q. For instance, if we will go to Pluri-B which is reflected on Government's Exhibit 2 in evidence, you

(Testimony of Russell R. Bavouset)

note that [153] it says "riboflavin 2 mgms." or two milligrams per cubic centimeter. Can you find anything on there which shows that that is in an aqueous solution?

A. Other than the fact that it says "sterile solution." It doesn't say "aqueous".

Q. There is nothing there to inform a doctor that it was in the type of solution that you have testified to, is there? A. No.

Q. And that is the substance which is reflected by the vials here, Government's Exhibit No. 1, a portion of Government's Exhibit No. 1; isn't that correct?

A. That is a portion.

Q. That was the label that was on?

A. Oh, yes. That is the type of label we would put on such a product.

Q. Now, thiamine hydrochloride, I think you state, does under some circumstances, according to your understanding, have some deteriorating faculties; that is correct, isn't it? A. That is right.

Q. You were selling this to doctors and you made this batch in the fall of 1945, did you not?

A. That is right.

Q. And you did not anticipate selling that batch within maybe one week or two weeks, did you? [154]

A. No.

Q. You intended to keep that amount or that amount that you had put up until in the current course of events it had been sold, or until it had been on your shelves for maybe too long, and then you would remove it, didn't you? A. That is right.

(Testimony of Russell R. Bavouset)

Q. And you kept it on shelves just like we see in drug stores, did you not? You did not have it in an ice box or anything like that? A. That is right.

Q. You expected that the doctor who would buy this product would take it out of this rather unique sponge rubber thing by the injecting device that he had, did you not? A. Yes; per the hypodermic needle.

Q. Per the hypodermic needle.

A. With a syringe.

Q. You were aware from your experience in manufacturing these products that a doctor might keep such a product as this for many months before he would use it, were you not? A. He might.

Q. You were aware of the fact that formerly, until this sponge rubber device was developed, that normally doctors used to buy many of their intravenous solutions in little ampules that they would break just to give one; that there would be just sufficient for one injection? [155] A. That is right.

Q. It was your contention that this, maybe, contained 30 to 40 times as much as any of these little ampules; isn't that true? A. Yes; that is right.

Q. And you anticipated that a doctor might have retained this bottle for some time until it had served its purposes; isn't that true?

A. That would be true.

Q. Now, did you think that it was important to caution the doctor about this product or any other product to the effect that this thiamine hydrochloride was a rapidly deteriorating product or was a deteriorating product?

A. It is not a rapid deteriorating product under ordinary circumstances, that is, in solution.

(Testimony of Russell R. Bavouset)

Q. Then you felt that it was sufficiently stable, that even a year after you had made it, it still ought to be in good shape and would be efficacious in the amounts as your label indicated; is that correct?

A. It might have deteriorated some. I would not say a great deal in that length of time. [156]

* * * * *

Mr. Stick: May I be permitted at this time to say that I would like to withdraw the position I took yesterday with reference to the authority of the inspectors to examine the records or the shipping receipts? I think it is only fair that I should do it at this time, so that I will not take up the time of the court.

Mr. Neukom: Thank you.

RUSSELL R. BAVOuset (Recalled)

Cross Examination (Resumed)

By Mr. Neukom:

Q. Merely by way of example, Mr. Bavouset, would you look at the cork or the stopper, whatever it is called, for instance, on Government's Exhibit No. 8, and the plastic seal around this, and then it is sponge rubber. From your understanding and from your experience, using that as an example, is that not considered to be one of the latest or the most improved methods of corking and sealing products of all of the characters that are involved here? A. Yes; that is one of the methods.

Q. And that has proved to be quite satisfactory; that is to say, does not allow impurities to get in, to your [160] knowledge; isn't that correct?

A. Yes; that is.

(Testimony of Russell R. Bavouset)

Q. And retards light, of course, from getting in and keeps the contents in a reasonably good state of preservation; isn't that correct?

A. That is correct.

Q. And the bottle itself of the character of No. 8, and likewise the other bottles which, from appearances, are the same, is of an amber color; and I have noted and I believe and am going to inquire of you if it is not true, that it has been found that an amber colored glass of this character has a tendency to assist in retaining the quality of the product that is placed in it, does it not?

A. Yes; in those products where light causes damages.

Q. To your opinion, these bottles are of approved and most proper shape to be used in placing any one of these solutions that you were offering for distribution, are they not? A. I believe they are; yes, sir.

Q. Now, taking up the substance "Indoform" here, as I understood your testimony to be, that you placed in this vial when you made up the amount which was to be vialled—if that expression might be used—

The Court: Do you use that synonymously with "bottled"?

Mr. Neukom: "Bottled", that is the word I wanted and [161] it didn't come to me.

Q. About how many bottles or vials do you recall manufacturing shortly prior to the date of the shipping of the Indoform involved in this case?

A. That is the total number of vials manufactured up to this time?

(Testimony of Russell R. Bavouset)

Q. No; the amount that constituted the pre-bottling that went into the shipment of around September 17, 1945.

A. The amount that was made up at the time this particular material was made up, is that it?

Q. Yes; that is the point there.

A. I do not have the records on that. At that time, it seems to me that we were making between two and three litres at a time, or would run somewhere between 65 and 100 vials.

Q. And that product was mixed, or whatever its chemical work, was done by you, is that correct?

A. That is correct; yes, sir.

Q. And likewise, the product involved in this case, that is to say, the amount prior to the shipping of Pluri-B, as I recall, you likewise prepared that, did you not?

A. That is right; yes, sir.

Q. And the product that is designated as "Vitamin D", you likewise handled the manufacturing or the placing together of the constituents there? [162]

A. Yes. The compounding, yes.

Q. Compounding, that is the word. And the product which is known here as the sterile solution, likewise, and Pluri-B, as I recall, in Count VII, you handled the making of that, the product which we now observe has the cloudy or precipitated particles in it?

A. That is right.

Q. May I just inquire, you are not a chemist, are you, Mr. Bavouset?

A. I am not a graduate chemist; no.

(Testimony of Russell R. Bavouset)

Q. But you have had years of experience, of course, in this kind of work, haven't you?

A. That is right.

Q. And have made a great many products, I assume, in those years of experience?

A. That is right.

Q. You are likewise not a pharmacist, are you?

A. No, sir; I am not.

Q. Then, I take it you did not graduate from schools in either of those trades?

A. I am not a graduate of any university.

Q. I see. Our father was quite a good druggist, but neither was he a graduate of any university. May I inquire now, Mr. Bavouset, with respect to this Indoform again, as is reflected from Government's Exhibit No. 4? You [163] stated to me that the label was a matter which you had prepared; that is correct, isn't it?

A. That is correct.

Q. And you, of course, expected this label to be read by men who were trained in the medical field and who had knowledge of pharmacology or the constituents of various types of medicine or more recent foods which some of these B products are called; isn't that correct?

A. That is right.

Q. And when you used the term "thyroid substance" there, it was your understanding that the practicing physician and surgeon would naturally believe that that denoted a thyroid substance as might be reflected in the Pharmacopoeia; isn't that correct?

A. No; that is not.

Q. Well, now, do you know of any thyroid substance that a physician might care to use, even combined with

(Testimony of Russell R. Bavouset)

other compounds, that he would desire to use unless it had some therapeutic value?

A. Well, I have talked to doctors about this thing and I know that—they have expressed opinions about the activity, etc., and there is a great deal of variation in the minds of the doctors what is accurate and what is not. I am not a pharmacologist so I can't tell you straight off.

Q. Mr. Bavouset, the posterior pituitary, you know, has some therapeutic value, has it not? [164]

A. Yes.

Q. And the other essential or individual components of this product have? Whole ovarian, that was not a meaningless product, was it?

A. Well, I didn't manufacture it to be.

Q. It was your intent that it had some value to be used in the human body, was it not? A. Yes, sir.

Q. Now, when you used the words "thyroid substance" didn't you think it would be only proper and advisable for you to advise on your label the doctor that this was a product with negative value and did not contain any of the iodine constituents which are normally in the thyroid?

A. Taking into consideration the rules and regulations, I thought it would be advisable to advise them that way; yes, sir.

Q. Well, you have pointed out on the bottom of that label that all of the products apparently have no therapeutic value; isn't that correct?

A. In this particular solution, this form would not be measureable.

(Testimony of Russell R. Bavouset)

Q. Now, just what was it that the thyroid did contain, if it did not contain any of the iodine?

A. Well, as I say, there is a great deal of variation in the opinions of medical doctors, even in the medical [165] schools, as to what does compose thyroid. There is a measurable substance in thyroid known as thyroxin, and it is generally considered the active ingredient. But I have talked to many medical doctors who claim that there are other activities that can be attributed to thyroid other than the activity of the thyroxin itself.

Q. Isn't it true the iodine that is in thyroid is there from what—not I—the chemists consider an organic source, that is to say, it comes into it as a result of body action rather than from an artificial placement?

A. That is correct.

Q. That is true, isn't it? A. Yes, sir.

Q. And that it be free from an inorganic source, that is, taking the salt itself and placing it in, rather than nature doing it; isn't that correct?

A. That is right.

Q. Were you not familiar with the Pharmacopoeia which gives the definition of "thyroid", turning to page 503 of the 12th Edition? A. Yes; I was.

Q. And it reads, does it not: "Thyroid is the cleaned, dried and powdered thyroid gland previously deprived of connective tissue and fat." With that you agree, is that not true? [166]

A. That is correct; yes, sir.

(Testimony of Russell R. Bavouset)

Q. Did your thyroid gland have the connective tissue and fat in it, or do you know?

A. Well, all the material that I purchased was purchased already dessicated, and I believe it was well defatted. We checked the content, etc., and I am quite sure it was as described by the U. S. Pharmacopoeia.

Q. "It is obtained from domesticated animals that are used for food by man. Thyroid contains not less than 0.17 per cent and not more than 0.23 per cent of iodine in thyroid combination." Is that correct?

A. That is correct.

Q. "And must be free from iodine in inorganic or any form of combination other than peculiar to the thyroid gland." In other words, as I previously questioned you, it must be free of inorganic, coming from a foreign source, to be a thyroid substance; isn't that correct?

A. To be a thyroid iodine it must be.

Q. And carrying on further: "A dessicated thyroid of a higher iodine content may be brought to this standard by admixture with a dessicated thyroid of a lower iodine content or with lactose, sodium chloride, starch or sucrose." You agree with that statement in the Pharmacopoeia, do you not?

A. That is right. [167]

Q. And yet, Mr. Bavouset, is it not true, then, when you place on a label the designation "thyroid substance" that you are doing so, knowing that medical men will read that and will assume that the product contains the same as the definition of "thyroid" as is reflected in the Pharmacopoeia that I have just read to you?

A. I did not do it with that intention. I did not feel that that was the way it would be.

(Testimony of Russell R. Bavouset)

Q. You knew that the medical man obtaining this thyroid was not getting the thyroid with the iodine content?

A. The medical man who would take a solution of thyroid would ordinarily know, I am sure, that he would not have iodine present.

Mr. Neukom: Just my question again, if I may, and then you, of course, can explain it.

* * * * *

A. That is right.

Q. Now we will look at Government's Exhibit No. 4, as we did at some of the others yesterday. There is nothing on that label, is there, nor was there on the vial anything cautioning a doctor as to any unusual precautions which should be indulged in in relation to this product?

A. No, sir.

Q. Now is there anything on the label telling the [168] doctor that any of the products might lose their efficacy with a reasonable period of time?

A. No, sir.

Q. This statement seems a little singular to me and I would like to have you explain it, if the court is interested: "This preparation does not contain any known therapeutically useful constituent." What was the significance of that statement?

A. Well, in the first place, the Pure Food and Drug rules and regulations made it necessary for any product that did not have a known standard, as set forth in some of our standard books, such as the United States Pharmacopoeia, national formula, etc., if they did not have a known standard, that it would be necessary to put a disclaimer on. This was followed throughout the

(Testimony of Russell R. Bavouset)

industry. First, as I remember, it was sold as "whole ovarian," and we would say, "no estrogenic precipitation present," etc. That form was changed several times. This particular statement here, being a disclaimer, meaning that we do not know of any particular test which would prove the potency of this product, was put on there for that purpose.

Q. But you were not selling it, of course, as an entirely futile product? I mean as just like a handler of distilled water, of course?

A. No. That particular statement was put on there [169] due to the fact that we were trying to conform to all rules and regulations and, at the same time, give the doctors what they wanted.

Q. In your opinion, this preparation "Indoform" reflected by the label of Government's Exhibit 4 for identification, if there were anterior pituitary 30 grains per each cubic centimeter in the product when you combined it, and had it received just normal care, temperatures of rooms and all, three months or six months from that, that same amount should have been in the vial, should it not?

A. That is right.

Q. And it would not have deteriorated rapidly?

A. Yes. That is the anterior pituitary you are speaking about?

Q. Yes; referring to that and that alone.

A. Yes, sir.

Q. Referring to the thyroid substance, your answer would be the same as to that?

A. That is right; that is right.

Q. With respect to Government's Exhibit No. 2 for identification—I believe we covered this, but I will try

(Testimony of Russell R. Bavouset)

to hasten along—the Pluri-B, the thiamine hydrochloride—50 milligrams per each cubic centimeter, had there been that amount in there when you combined it, six months from then, had that bottle been retained, had the seal been retained on [170] there and no unusual factors entered into it, approximately that amount should have remained in the solution, should it not?

A. That is right.

The Court: Are you referring to Exhibit 2 for identification?

Mr. Neukom: I am referring to Exhibit 2 in evidence. I read the upper one but I did not look at the bottom, your Honor, and I will say that inadvertently.

* * * * *

Q. May I inquire, Mr. Bavouset, did you have any of the basic materials that went into any one of these four—I think there are three—three different solutions or compounds, prior to compounding the individual allotment or allotments, did you have them assayed? [171]

A. Other than labeled potency, as I purchased it from the manufacturer, I can think of but one that I had assayed, and that would be one that I made myself. That would be the posterior pituitary. I do not have the exact batch of material that I made at that time available; that is, I do not remember it, it has been so long ago. But at that time I was making the posterior and still am making the posterior pituitary myself, and at that time the biological process was completed and I then sent that assay out for a batch assay of the posterior pituitary itself. That is not an assay of the Indoform; that is just the posterior pituitary.

(Testimony of Russell R. Bavouset)

Q. But you do not recall whether the product that went into the Indoform reflected in Counts I or II here—

A. No.

Q. —was assayed prior?

A. Only as I said, the posterior pituitary, I know, when I used it was up to standard. I diluted that, of course.

Q. As a matter of fact you did not have that particular posterior pituitary assayed, did you, that went into this allotment here?

A. Yes; I did.

Q. Have you brought that assay with you?

A. No. It would be impossible for me to say which batch went into it. In other words, I have a large batch of posterior pituitary which I make up, we will say, approximately [172] 20 units. I have that assayed and then use it on that basis.

Q. The finished compounded preparation of any of these three here, then, you can explain further, that if any of these four drugs here, including the sterile matter which has the suspended particles in it, did you have any assays conducted on any of the finished product?

A. Does that include that particular product there that has come down in precipitate?

Q. Yes; it includes that, too.

A. I unfortunately did not bring the assay card on that, as the matter of the potency was not involved here. I did not bother with it. The other products I did not have because the facilities were not available at that time. But I am quite sure I have an assay card on the material. It is all being assayed at the present time, and I am quite sure that I do have an assay card.

(Testimony of Russell R. Bavouset)

Q. That is a card back in 1945? Did you have an assay run on it shortly after you had compounded it?

A. No.

Q. Then you had sent the amount of it to Dr. Ryerson—
A. Was that in 1945?

Q. I will get the date. '46. You had sent the quantity designated to Dr. Ryerson on June 18, 1946 prior to [173] conducting any assay upon the sterile solution of Pluri-B, had you not?

A. No; there was an assay run on that.

Q. Have you brought it with you?

A. No. I am sorry I did not bring it. As I said before, the amount of the matter of potency did not come up in that particular case.

Q. Didn't you think that would be rather important in connection with this matter, Mr. Bavouset?

A. I did not, inasmuch as the potency had not been involved.

Q. Weren't you concerned; weren't you getting any complaint, even, from Dr. Ryerson about the suspended particles in that matter?

A. No. Dr. Ryerson did not complain about that particular shipment.

Q. He did not complain directly? A. No, sir.

Q. The thiamine hydrochloride that went into this Pluri-B, as reflected from Government's Exhibit 2 for identification, did you have that assayed, the basic product?
A. No, sir.

The Court: That is Government's Exhibit 2, the label?

Mr. Neukom: Yes, your Honor; the label.

(Testimony of Russell R. Bavouset)

Q. And did you have assayed the thyroid substance [174] that is contained in this Indoform? Did you have that assayed?

* * * * *

A. No, sir.

Q. Do you recall that you were present at a hearing, at an administrative hearing, of the Food and Drug Administration conducted in conjunction with this investigation, and appeared on or about November 7, 1945 before Mr. Rowe, the gentleman who is writing here, sitting next to me, and they were investigating a matter concerning some of these products here, and particularly the Pluri-B that is referred to in this case in Counts III and IV—this matter is not upon the file—didn't you state to Mr. Rowe at that time that your more recent investigation indicated that this particular shipment could have had a deficiency in Vitamin B-1, the thiamine?

A. I am very sorry, I can't remember such a statement.

Q. Do you recall that you were present on or about April 23, 1946 in a Food and Drug Administration hearing conducted before Mr. Gray? Is Mr. Gray here? Will you stand up? Do you recall that gentleman?

A. Yes; I do.

Q. And that is with reference to the product which [175] became the subject matter of Counts I and II, the Indoform, and that you stated that you had had that solution later tested by the Cooper Laboratories who found it contained such small quantities of posterior pituitary as to be immeasurable?

A. That is right; I did that.

(Testimony of Russell R. Bavouset)

Q. And that is, of course, after you had shipped the product? A. That is right.

Q. And did you not likewise state to Mr. Rowe at the hearing on or about November 7, 1945 with regard to the Pluri-B and the thiamine deficiency, that you did not have the equipment to make the thiachrome determination for thiamine and that you would have to, therefore, revise your manufacture and procedure?

A. We did not have the equipment. Now, about the revision of manufacturing procedure, that goes on almost every day. [176]

* * * * *

Q. Is it not true that, with regard to the undissolved particles in this Government's Exhibit No. 1, the product shipped to Dr. Ryerson, that you yourself only examine for undissolved particles at the time that you make the product? A. No; that is not true.

Q. Mr. Bavouset, do you subscribe to the testimony as reflected by Dr. Wiley, that this product contained 20 times the amount of riboflavin—

A. I recall his testimony.

Q. Yes. —that can be hoped to be dissolved in an aqueous solution? Do you subscribe to the statement, or do you have a variable thought on that?

A. I would like to qualify it.

Q. Surely, you may. [177]

A. I have examined the products manufactured of all my competitors—not all my competitors, but many of them, and I believe, right in court today, we have one that contains four milligrams of riboflavin per cubic centimeter, in competition with our product, which would be 40 times. The fact that one-tenth—let's see; that

(Testimony of Russell R. Bavouset)

would be about one-tenth milligram per cc, soluble in ordinary water solutions, would have to be considered in the light that nicotinamide is a very fine solvent for riboflavin, and that when you put riboflavin in a solution with nicotinamide it will aid a good deal.

There are other substances, salts, that are recommended by the manufacturers of riboflavin. I have correspondence of those manufacturers that these salts aid the putting into solution and stabilizing in solution riboflavin.

That has been a major problem with all manufacturers, and much discussion and much writing has been done upon the subject.

The Court: Is it your opinion that the precipitate in those two bottles which are part of Exhibit 1—are they not Exhibit 1?

Mr. Neukom: Yes, your Honor; they are a part of Exhibit 1 and the label is Exhibit 2.

The Court: Is it your opinion that, whatever that substance appears to be precipitated in that liquid, is a [178] precipitate of riboflavin?

The Witness: Yes, your Honor; it is my opinion. I can't say that entirely, but that is my opinion.

The Court: And that would be due to the excessive amount of riboflavin over and above what would dissolve in the solution?

The Witness: Not necessarily, your Honor. That might be due to varying conditions of weather. I have noticed it come down upon fluctuation of temperature. Putting into warm water, very often that type of thing goes back into solution or remains that way. It is rather common. We have had that happen. Even some manufacturers go as far as to state on their label: "In case

(Testimony of Russell R. Bavouset)

riboflavin precipitates, warm until it goes back into solution."

Q. By Mr. Neukom: Then it is your position that nothing, of course, has been added to either one of these bottles other than what you put into them. Let us, you and I—

A. I take that stand.

Mr. Neukom: Let us take the cork here and cut off this seal.

The Witness: I don't believe there is any reason for—

The Court: You are taking off the seal of one of the bottles comprising Exhibit No. 1?

Mr. Neukom: Exhibit No. 1, your Honor, so that we may see the rubber cap as well as we can. Of course, a little paper [179] adheres to it.

Q. But it has the indications, does it not, that nothing has been added to the product?

A. It has that indication. I couldn't say, of course, but I would take the stand that it does not have.

Q. And you do not advise, by your label or otherwise, the prospective user of this product that such a condition might occur?

A. No. I had not expected it to occur and for that reason had not advised them.

Q. What has been your experience as to how soon after the compounding of this product that that condition does occasionally occur?

A. Sometimes those vials will go for six, seven or eight months and then nothing ever occurs to them. Then sometimes we will get the refrigeration extremely low temperature, a break in the weather, that is, and a portion of the riboflavin content comes out in a precipitate.

(Testimony of Russell R. Bavouset)

Q. Could it be other impurities? It is riboflavin, or would you want to express an opinion?

A. I don't know. I really couldn't say. I don't believe so.

Mr. Neukom: I see. I think that will be all.

The Court: Would it be your opinion that a lesser amount of riboflavin would be less likely to precipitate? [180]

The Witness: Yes, your Honor; I would be of that opinion. As I have said, I have examined the products of many of my competitors and I have found that precipitates come out even in lesser amounts, that is, even in lesser concentrations, sometimes, and they still come out where, perhaps, the other type of salts that are good for stabilizing have not been used. I couldn't say what they are using, but sometimes a small amount of riboflavin comes out due to its insolubility, the same as a larger amount. It has been a major problem.

The Court: Is there some definite purpose in including in one of the Pluri-B products only one milligram of riboflavin per cubic centimeter and, in the other, two milligrams?

The Witness: Yes, your Honor. The intramuscular as I said, it was quite stable and we had a lot of success with it. And then we put in two milligrams. Perhaps I was a little optimistic, I don't know, and we had a great deal of good fortune with that at all times, and upon a very rare occasion something like this did happen.

The Court: I notice apparently that the label for the product containing only one milligram of riboflavin states that it is for intramuscular use, whereas the label of

(Testimony of Russell R. Bavouset)

the product Pluri-B which contains two milligrams of riboflavin states for intramuscular or intravenous use.

The Witness: Yes, your Honor. The intramuscular use [181] material here, the multiple dose vials, where they are punctured many times, that has been frowned upon for intravenous use by some physicians; and we had taken a stand that it was usually to be used for intramuscular use only.

Later on, it seems to have become very well recognized, at least it is common practice to use material from vials in intravenous use.

We checked to see if other manufacturers were using for intramuscular and intravenous use both materials where intravenous use may be indicated, and we found they were using that type of labeling; so we included that in our particular product.

The Court: What I was attempting to arrive at, what would be the reason for a product called Pluri-B, containing one milligram of riboflavin per cubic centimeter that would be labeled "for intramuscular injection," and another product, the same product, containing two milligrams of riboflavin per cubic centimeter, labeled "for intravenous or intramuscular"?

The Witness: There is really no reason for that, other than the fact that in the length of time between the two we had noted that our competitors were using it for both intramuscular and intravenous use, that is, similar products; and we felt that, inasmuch as it had become common practice, that we would include intravenous use as well. [182]

The Court: Is it your opinion that the Pluri-B with one milligram of riboflavin per cubic centimeter would

(Testimony of Russell R. Bavouset)

be just as efficacious as the same product with two milligrams of riboflavin per cubic centimeter?

The Witness: Yes; it would be.

The Court: And if it were to be used for intravenous injection, and there is danger of precipitation, it would be a safer product to have lesser riboflavin in it, would it not?

The Witness: Well, that is true to a certain extent, your Honor. I did not expect it to be that way, of course, originally.

The Court: Now with respect to the thiamine hydrochloride, would you expect if you put 50 milligrams in a cubic centimeter of product, would you expect it to dissipate in some way to where there would be only 33 milligrams per cubic centimeter a few months later, or even a year later?

The Witness: No, your Honor; I would not expect that.

The Court: Is there any reason you can think of why there would be less thiamine hydrochloride later than there was at the time it was manufactured?

The Witness: Well, those factors which have to do with the breaking down of thiamine, including the way it is kept, for one thing, the base, that is the alkaline or acid condition of the base in which it is in, anything that [183] influences that, then it breaks down much faster. .

There are certain factors involved there that we do everything we can to take care of, and expect them under normal circumstances to remain constant.

(Testimony of Russell R. Bavouset)

The Court: Have you had any experience with thiamine hydrochloride in a solution dissipating to the extent of a third or a half?

The Witness: Yes; a great deal, your Honor. And making these solutions, if we approach the neutral stage, we will say, where we have a pH. as high as 7, the material is not stable at all and, with a small amount of heat, dissipates very, very rapidly. So, for that reason it is necessary to keep thiamin hydrochloride in concentration up around 3.2.

The Court: You have been making this Pluri-B for sometime?

The Witness: Yes, sir, your Honor.

The Court: Have you had any trouble with the thiamine hydrochloride content becoming dissipated?

The Witness: No; not in Pluri-B as long as we watch our pH.

The Court: Well, what would cause it to dissipate, exposure to air?

The Witness: Well, that exposure to air could cause the dissipation of thiamin, your Honor. [184]

The Court: If the doctor takes one of these vials or bottles and he punctures the cap, the rubber cap, with a hypodermic needle to make an injection in the patient today, then he has a patient requiring more treatment next week, and another one next month, and another one two months later, would you expect the recurring punctures in that cork, that rubber cork, will admit air and cause the thiamine hydrochloride to dissipate?

(Testimony of Russell R. Bavouset)

The Witness: Yes, your Honor; that is a known fact, it will be done.

* * * * *

The Court: Would this cap here, this rubber cap, be a safe cap to use on this product where it is punctured time and again by a hypodermic needle?

The Witness: Yes, your Honor; it is considered a safe cap.

The Court: Is it supposed to seal itself?

The Witness: Yes, your Honor; it is expected to be self- [185] sealing.

The Court: That is all I have.

Mr. Neukom: May I have one or two questions.

Q. This thiamine hydrochloride product, the one which has the 50 milligrams in it, what base is that in? Is that in an alkaline or an acid base?

A. The thiamine hydrochloride, when it is put in solution by itself, is very acid.

Q. Which is Government's Exhibit 2, the label?

A. Yes, sir.

Q. Well, that is a proper base to retain the efficacy of that vitamin product, is it not?

A. The acid base is the proper base,

Q. I would like to ask one thing on this cork, but not staying on it too long. When the hypodermic needle is placed in it, why, it seals, by the soft cork, all air from going in and merely allows the needle to go down, doesn't it?

A. It will stand to reason that it is impossible to take that vial and put a hypodermic needle in it and pull out a certain amount of solution, pull the hypodermic needle out,

(Testimony of Russell R. Bavouset)

and expect that to continue to form a vacuum. About the third time you place that hypodermic needle in there and pull it out, you will have a little trouble. The vacuum created inside that vial will cause a little difficulty in filling the plunger and it will be necessary to pull the plunger back and forth. It is common practice to place the [186] needle back in, pull out the air and let it run out.

Q. You buy your thiamine chloride in a bottle, don't you? A. Yes; or it comes in a powdered form.

Q. And that bottle has a screw cap on it, doesn't it?

A. Well, it comes in all different types. It is sealed up on the top and usually comes in carboys or drums.

Q. You do not always use all the product when you get it, do you?

A. We try to at once. That is, when you open a carboy that has been sealed up, we try to use the whole thing at one time.

The Court: Do you mean a 10-gallon jar?

The Witness: A carboy is like, we will say, just a container that contains usually one kilo, 1,000 grams.

Q. By Mr. Neukom: You did not use up a thousand grams when you made this product here that supposedly has the 500,000 units?

A. Working with Vitamin D there, sir.

Q. Oh, I beg your pardon. The one that had the thiamine chloride here.

The Court: 50 milligrams.

Q. By Mr. Neukom: 50 milligrams. You did not use up a whole can of it in compounding that allotment, did you? A. Yes; we generally do. [187]

(Testimony of Russell R. Bavouset)

Q. Well, you do not throw it away when you have some left, do you?

A. Not by any means. We usually compound a sufficient amount in a day to use up the entire amount at the time.

Q. But some sets around on your shelves, doesn't it?

A. A very short length of time.

Q. But it is your testimony these are rather a thick kind of rubber caps, aren't they; they are not just like a little sheet of rubber, are they?

A. That is particularly thick.

Q. They look like a quarter of an inch thick?

A. They are so thick they will seal off and keep air out even though a vacuum is formed inside.

Q. Do you mind if we take one of them?

A. I do not; no, sir.

Mr. Neukom: Do you, counsel?

Mr. Stick: I have no objection.

The Court: If there is a danger of air entering the bottle with treatment, intermittent use, that is, treatment with intermittent insertion of the hypodermic needle, should there not be some warning on the label that these properties such as thiamine hydrochloride are likely to become dissipated through entrance of air into the bottle over a period of time?

The Witness: It possibly would be a good suggestion, your Honor, to have a label stating that it should be used up [188] very rapidly after first puncturing.

The Court: In this product would it be harmful if it had twice as much as 50 milligrams of thiamine hydrochloride?

(Testimony of Russell R. Bavouset)

The Witness: No, your Honor. We have products, and there are many products on the market, that contain 100 milligrams of thiamine hydrochloride per cubic centimeter.

The Court: If you put more in than the label states, in order to be sure that at all times it has the labeled strength, there would be no harm could come from it?

The Witness: No, your Honor; there would not be.

Mr. Neukom: Your Honor may care to see what the cap is like. The plastic has been removed from it. There is a little paper adhering to the top of it.

The Court: The space intended for the insertion of the hypodermic needle is comparatively small in proportion to the surface of the cap, is it not?

The Witness: That is correct, your Honor; very small.

The Court: How many injections would this bottle hold, about?

The Witness: The average injection is about one cubic centimeter; so that would be approximately 30.

The Court: 30?

The Witness: Yes, your Honor.

The Court: How many times would you think a doctor could insert a hypodermic needle in the space provided here [189] in this cap before there would be a hole in it?

The Witness: Well, I have been given to understand it will go up to 100 times, though I have never tried it personally.

Q. By Mr. Neukom: At least, it should go more than the contents of the bottle? A. Yes, sir.

The Court: And is it your opinion that it will?

The Witness: Yes; it is, your Honor.

Mr. Neukom: That is all.

(Testimony of Russell R. Bavouset)

The Court: And unless there is some interference from the outside, presumably there would be no air enter the bottle to dissipate the thiamine hydrochloride?

The Witness: No, your Honor; there would not be.

Redirect Examination

By Mr. Stick:

Q. This type of cork or stopper is the common type in use in the industry for the handling of these kind of products? A. It is the common type.

Q. When you withdraw a cubic centimeter of liquid from a bottle, does that not create a vacuum to an extent?

A. That does create a certain vacuum; yes, sir.

Q. And when you withdraw another cubic centimeter [190] you would create still more vacuum?

A. Even more vacuum; yes, sir.

Q. After a while, if no air got in there, it would be difficult to withdraw?

A. It gets to the point where it cannot be withdrawn; that is right.

Q. Is it not a standard practice then, if you are going to withdraw a cubic centimeter of a material from a bottle corked as this, to pull the hypodermic syringe out to the one centimeter, cubic centimeter mark, then insert it into the bottle and then push your cap in, pull that much air in it and then hold it up so the air is at the top, and pull out your one cubic centimeter of the product?

A. That is true. It is the common practice to take the syringe, pull it back a certain distance, that is, the

(Testimony of Russell R. Bavouset)

plunger of the syringe, inject the air into it without creating a pressure in there, then merely turn it, for instance, down and letting the plunger be forced back to a certain part and pull it out for the injection.

Q. So that each time something was removed there would be air get into the bottle that had not been there at the time it was manufactured? A. That is true.

Q. Have you seen and been around medical offices while doctors were taking things from bottles of that kind? [191] A. Yes; many times.

Q. Is it a common practice to use more than one substance at a time in a hypodermic?

A. Very common.

Q. And when they do use more than one substance do they take the one substance out of one bottle and then continue the plunger back and let the air out from the extra part that is taken back and draw the substance in and mix them both in the same hypodermic?

A. Yes.

* * * * *

Mr. Neukom: Well, I would like to make this observation, if I may: It might save a little time. Your Honor, at this stage of the case there has been no evidence offered that the product examined by the experts had gone through any of these stages of repeated air going into them.

(Testimony of Russell R. Bavouset)

The Court: No. I probably led the case off onto that tangent. I was curious about this cork in the bottle.

Mr. Neukom: Very well.

The Court: I appreciate that the contention here is not based upon the supposition that something happened to the products in a doctor's office.

Mr. Neukom: Very well, your Honor. [192]

The Court: And, I take it with respect to the first six counts, at least, there is no issue as to whether the compound or liquid had any therapeutic value or not.

Mr. Neukom: We have no issue on that, purely the quantitative amount.

The Court: It is a question—

Mr. Neukom: Of whether the label says—

The Court: —of whether the product contains what the label says.

Mr. Neukom: That is the sole issue of the six counts.

The Court: And that is, as manufactured and as shipped.

Mr. Neukom: That is right, your Honor.

The Court: And specifically, as introduced into interstate commerce.

Mr. Neukom: That is right.

Mr. Stick: That is all. [193]

* * * * *

ROLAND N. ICKE,

called as a witness by defendants, being first sworn, was examined and testified as follows:

The Clerk: Please state your name.

The Witness: Roland N. Icke.

Direct Examination

By Mr. Stick:

Q. Dr. Icke, what is your occupation?

A. I am a director of research at the Pasadena Research Laboratories.

Q. Is your research in chemistry? A. Yes, sir.

Q. Any particular type of chemistry?

A. Organic chemistry, medicines, drugs.

Q. What is your educational background?

A. I received a Bachelor of Arts, a Master of Science, a Doctor of Philosophy degrees from the University of California at Los Angeles. I have had a year of medical training at the Medical School of the University of Southern California.

Q. Do you belong to any societies of the chemical [194] type?

A. Yes, sir. I belong to Alpha Chi, Sigma Alpha Epsilon, Alpha Kappa Kappa, Medical Fraternity, Sigma Chi national sorority, and American Scientific Affiliation, the American Medical Society.

Q. What experience have you had in research with reference to medical products particularly?

A. Aside from the research in connection with working toward my degrees in chemistry, I have had seven years of research in the pharmacology and chemistry laboratories of Dr. Gordon A. Alles in Pasadena. I have also had research experience at the Pasadena Research

(Testimony of Roland N. Icke)

Laboratories since February, 1946. I had one year of teaching experience as associate professor of chemistry and chairman of the department of chemistry at Westmont College.

Q. Are you familiar with the types of products that are in evidence here? A. Yes, sir.

Q. I will show you Government's Exhibits No. 6 and 7, No. 6 being a bottle or vial containing a solution, and the Exhibit 7 being a label from that, and upon that appears to be the words "PLURI-B". From that label or on that label appears the language "Thiamine Hydrochloride," I believe. A. Yes.

Q. That is commonly known as the B-1, Vitamin B-1? [195] A. Yes.

Q. Vitamin B-1, which actually is a food, isn't it?

A. Yes.

Q. Is that a stable product?

A. Under normal conditions it is.

Q. Under what conditions is it not a stable product?

A. Vitamin B-1 can be destroyed very rapidly if the solution is brought towards neutrality or on the alkaline side in a solution that must be kept acid in order to be stable. Also, it is susceptible to destruction by presence of sulfites, or it can be destroyed by oxidation, and in any of those cases that those agents were present which might cause destruction, any temperature above normal would speed the rate of destruction.

Q. You are familiar with the type of cork or bottle stopper that is used on these bottles that are in evidence?

A. Yes; I am.

(Testimony of Roland N. Icke)

Q. We have one bottle here open from which a cork has previously been removed. Have you made any test or examination to determine whether by visual examination with the eye, as you look at a bottle, you can tell whether that cork has been punctured or not?

A. Yes; I have tested that fact.

Q. What did you do and what was the result of that test? [196]

A. I took a bottle that had a fresh stopper on it, that I had reason to believe had never been punctured, and I looked at that under the microscope after first examining it superficially to determine if I could see with ordinary vision whether it had been punctured. Under the microscope I could not tell that anything unusual had happened to the stopper. It did not appear to have any hole in it.

Then, that stopper, I inserted a needle such as commonly used for hypodermic injections through that stopper, pulled it out and again looked at the stopper with my eyes and was not able to tell where the puncture had occurred. It had sealed, as nearly as I could tell, completely.

Then I took that same bottle, put it under a microscope and observed the top and, after a considerable difficulty, finally located the spot at which the puncture had occurred. There was evidence that a needle or some object had penetrated the cap.

The Court: Which bottle?

The Witness: The bottle which I tested experimentally in the laboratory to determine—

The Court: That was a new bottle?

The Witness: Yes.

The Court: It is not here?

(Testimony of Roland N. Icke)

The Witness: No. I feel, though, that that same thing would apply to any rubber cap, because I have looked at a [197] number of bottles which I have seen punctured with needles and, by looking at it just with the naked eye, you can't tell readily whether they have been punctured or not.

The Court: So you cannot tell by visual examination with the naked eye whether the corks in the two bottles comprising Exhibit 1 have been punctured?

The Witness: No; not unless there had been an extremely large needle used, and I am not even positive that I could then.

Q. By Mr. Stick: What will cause the oxidation of thiamine hydrochloride?

A. There are many oxidizing agents which are known to have an effect on thiamine hydrochloride. In the assay for thiamin, thiamin is subject to oxidation by potassium ferri-cyanide or some other material produced, thiachrome, which is an oxidation product, one of the inside products, at least, of thiamin.

There are other materials such as peroxides which, if introduced into a solution containing thiamin, might cause destruction.

Q. Are you familiar with the methods used by doctors in their offices? A. Yes, sir.

Q. In handling bottles, hypodermic syringes, etc.?

A. Yes. [198]

Q. Do doctors sterilize their syringes and needles before they take out doses of medicine from bottles of that kind?

A. It is the common practice to sterilize them; yes.

(Testimony of Roland N. Icke)

Q. And what things are used for that purpose?

A. Well, sometimes they use steam sterilization, or heating the things in boiling water. Others may use bichloride of mercury or various other bacteriacides. Also, it has become more and more common in recent years to use isopropyl solutions for sterilizing instruments.

Q. Before a bottle of that character is used for the purpose of withdrawing a dose of medicine is it customary to sterilize with some substance the cork before the needle is inserted?

A. Yes. The doctor usually takes a piece of cotton or gauze and wipes off the top of the cap with alcohol, isopropyl alcohol is often used.

Q. If any of that isopropyl alcohol was left in the needle and went into the bottle would it affect the content or the potency of the thiamine hydrochloride?

A. It might, because isopropyl alcohol is known to contain bacteriacides under many conditions. I have worked in a chemical laboratory at the time that discovery was made and observed the experimental work of the investigator, who showed that isopropyl alcohol often contained bacteriacides. [199] And I have also seen doctors taking solution to be injected from this bottle in which they have used isopropyl alcohol to sterilize their needle and syringe, and often, instead of drying the needle and syringe, they may just put the needle onto the syringe and move the plunger back and forth to pass a little air through it and get rid of most of the sterilizing agent. But I have seen them insert a needle into a bottle and which it was not completely dry, and because of their practice, introduce air into it. It would be possible for a

(Testimony of Roland N. Icke)

spray of a small amount of isopropyl alcohol, and, therefore, bacteriacide, to be introduced into that bottle.

Q. And would the amount that would be so introduced affect the thiamine hydrochloride in the bottle?

A. It would depend entirely on how much bacteriacide was in the isopropyl alcohol, how many injections had been withdrawn from the bottle, and how much bacteriacide was there just how much it would affect it. But even a small amount would affect it.

The Court: Immediately?

The Witness: The effect would start immediately; yes.

Q. By Mr. Stick: You have stated that air is injected into the bottle. Just what did you mean by that?

A. In order to prevent a vacuum in the bottle when withdrawing a needle, it is common practice to pull the [200] plunger of the syringe back to the mark at which you intend to take your solution, inject that equivalent amount of air into the bottle and then allow the pressure inside the bottle to aid in filling the syringe.

Q. Would that air have any effect on the thiamine hydrochloride?

A. Thiamin is susceptible to oxidation and air contains oxygen, so undoubtedly air would affect the stability.

Q. Do doctors at times use more than one substance in a hypodermic injection?

A. Yes; it is common practice.

Q. And in using that will you describe their method of getting the two substances or more substances into the syringe?

A. After their usual sterilization procedure, they will withdraw the plunger of the syringe back to the mark corresponding to the amount of the first solution they

(Testimony of Roland N. Icke)

intend to withdraw, and they will insert that needle into the cap and inject into that bottle that amount of air; then they will withdraw that solution into the syringe and withdraw the needle from the cap, and then will withdraw the needle or the plunger of the syringe farther back to correspond to the additional amount of material which they wish to take, then will insert that needle into the second bottle and inject the air in that bottle and then withdraw from the second bottle. [201]

Q. By that could any substance get into a bottle containing thiamine hydrochloride that might affect it?

A. It could very easily happen. Thiamine hydrochloride is only put up in acid solutions, pH. around 3.2 or thereabouts. There needs to be acid in order to maintain its stability. If a doctor chose to give an injection in which, for example, he was using sodium salt of Vitamin C or some other material which was more alkaline in nature than the B complex, if he withdrew this more alkaline solution first into his needle, into his syringe, and then injected air in intending to withdraw his second sample, if he injected some air into that second bottle, there would be some of the first solution remaining in the needle; so there would be a very good chance; in fact, it would be practically certain that some of the first solution would get into this bottle of the second solution.

Q. That could affect the potency of the thiamine hydrochloride?

A. That could affect the pH., affect the degree of acid.

(Testimony of Roland N. Icke)

Q. And if the acid is raised, the destruction of the potency would increase?

A. If the pH. is raised, the destruction rate would increase.

Mr. Stick: Your Honor, we have used in this case a [202] number of times the "pH." Are you familiar with what that is?

The Court: I am not sure whether I am or not.

Mr. Neukom: I am not.

Q. By Mr. Stick: Doctor, would you, below this diagram here, and with some chalk that we have—

Mr. Neukom: There is some right up there.

Q. By Mr. Stick: Would you draw a graph, illustrate what this pH. is supposed to be and how?

A. "pH." is a measure of the degree of acidity, the base acidity of a solution normally.

The Court: And it is a departure from neutrality, is that it?

The Witness: There is a specific pH. in water for neutrality. That pH. is 7. (Diagraming.) If I let this roughly represent the pH. scale, pH's. vary from one through 14, for example. Any pH. between 1 and 7 is acid, considered to be an acid solution. Any pH. above 7 is considered to be an alkaline solution; a pH. of 7 would be a neutral solution.

Vitamin B-1, if kept at a pH.—Vitamin B-1 solutions are kept at a pH. normally around 3.2, which is definitely acid, because it is stable at that pH. If that pH. is raised, though, by the injection of any alkali, then its stability is less.

The Court: As it trends toward an alkaline substance, [203] is it?

(Testimony of Roland N. Icke)

The Witness: Yes; as it becomes more alkaline it becomes less stable.

Q. By Mr. Stick: And as it becomes more alkaline does the rate of destruction increase?

A. Yes; considerably.

Q. Doctor, if you will look at the label of the exhibit you have before you, the bottle 6 and the label 7, you see on the label "riboflavin 1 mgm.", is that correct?

A. Yes.

Q. You see "Nicotinamide", is that it? Is that the correct pronunciation?

A. Is this 7? Yes. Yes; I see the word "Nicotinamide".

Q. And that is 50 milligrams? A. Yes.

Q. There is also—how do you pronounce this?

A. "Pontochenic acid, pyridoxine hydrochloride, riboflavin and thiamine hydrochloride," as well as the nicotinamide.

Q. You were here when the Government's chemist stated his method of analyzing the contents of Exhibit 6 for the purpose of determining the potency of the thiamine hydrochloride? A. Yes.

Q. Would you state that that test is a fair test in [204] the light of the other ingredients which are in that bottle?

A. It is generally considered as being reliable within certain limits of error.

Q. Would the nicotinamide have anything to do with the solubility of the riboflavin?

A. Very definitely.

(Testimony of Roland N. Icke)

Q. Will you describe what you mean and what action would take place?

A. Nicotinamide is known to increase the solubility of riboflavin. In fact, there are other ingredients also which make riboflavin more soluble than it would be in water alone; so that when you are dealing with a solution containing other things besides riboflavin and water, there really is no good measure of just what the solubility of riboflavin is in terms of its water-solubility, because water is no longer your solvent. You have a solution containing these other things which is your solvent. The solvent is not the pure water.

Q. Would the presence of the nicotinamide and, perhaps, the other substances increase the amount of riboflavin that could be dissolved into a product.?

A. Yes; very definitely.

Q. A definite amount of solution?

A. Yes. I have seen products on the market which contain as much as five and three-tenths milligrams of riboflavin per cc, when other ingredients in those were present, [205] and have in my possession a sample purchased on the open market which contains four milligrams per cc of riboflavin.

The Court: A clear liquid?

Q. By Mr. Stick: And does that also contain thiamine hydrochloride?

A. I believe so. It contains 10 milligrams of thiamine hydrochloride, four milligrams of riboflavin, and 20 milligrams of niacinamide per cc.

The Court: Does it contain any nicotinamide?

The Witness: Yes, sir.

(Testimony of Roland N. Icke)

The Court: Is it a clear solution, without precipitation?

The Witness: It has some precipitation. It is very difficult to detect. The amount is considerably—is a very small amount.

Q. By Mr. Stick: Would you say that the formula set forth on the label, Exhibit 7, which was on the exhibit bottle, No. 6, contains an undue or unreasonable amount of riboflavin in the light of the other ingredients that are contained in the solution? A. No.

Q. Are you familiar with the general practice of doctors in the handling of their medicines and so forth in their offices? A. To a certain extent; yes.

Q. You have been in medical offices? [206]

A. Yes; many of them.

* * * * *

Q. Is it customary when one of these bottle like we have here, containing, say, 30 cubic centimeters of a product, when it has been used, say, once or twice to throw it away?

A. No. The doctor puts it on his shelf, ready for [207] use next time.

Q. Do they ever deliberately insert other things into bottles to make a different combination of a product?

Mr. Neukom: Your Honor, I will stipulate that they do.

Mr. Stick: All right; that is all I asked for.

The Court: Very well.

Q. By Mr. Stick: Turning to Exhibit Nos. 3 and 4—your Honor, while we are on this same subject of the Pluri-B, I will withdraw this 3 and 4 and show the wit-

(Testimony of Roland N. Icke)

ness Nos. 1 and 2, because it is substantially the same product and the testimony would be more or less along the same line, I would imagine.

Will you examine those bottles as to their content? What do you observe by examining the bottles?

A. There is a precipitate in it.

Q. I will ask you to examine the labels on Exhibit No. 2 and you will find there, I believe, riboflavin 2 milligrams, is that correct? A. That is correct.

Q. What other products are in that solution besides the riboflavin?

A. This solution also contains 50 milligrams of the thiamine hydrochloride, 10 milligrams of pyridoxine hydrochloride, 10 milligrams of pantothenic acid, and 50 milligrams of nicotinamide. [208]

Q. Now, save for the riboflavin, the ingredients and the amounts of the ingredients as shown on Exhibit 2 are the same as shown in Exhibit 7 which you had before you a few moments ago?

A. I believe that is correct.

Q. The riboflavin, however, has one milligram more than it did in the Pluri-B which you have been testifying to heretofore under Exhibits 2 and 3, I believe?

* * * * *

The Court: Exhibit 6, the label to Exhibit 6 is Exhibit 7, which contains one milligram of riboflavin; and the Exhibit 1—

Mr. Stick: Now he has 1 and 2 before him.

The Court: Yes. They contain two milligrams, as I understand it, is that correct?

The Witness: That is correct.

(Testimony of Roland N. Icke)

Q. By Mr. Stick: And other than that, they are apparently the same, is that correct? A. Yes.

Q. Now, would you say that in the light of the substances contained in the bottles before you, Exhibits 1 and the label 2, that the two milligrams of riboflavin was an excessive amount?

A. No; I would not. [209]

Q. Did you hear Dr. Wiley's testimony with reference to that? A. Yes.

Q. I believe that he made the statement that that was a supersaturated solution of riboflavin?

A. Yes.

Q. Would you call that a supersaturated solution of riboflavin? A. No; I would not.

Q. Will you state why?

A. Because I have seen other products containing more than that much riboflavin which did not have a precipitate in it; and also, because I have seen products containing less which did have a precipitate in it; so it is apparent to me that some other factor must be involved.

Q. In examining the bottles in Exhibit 1 and observing the precipitate that you find therein, would you be able to state when that precipitate occurred in that bottle? A. Certainly not.

Q. Could you say whether the precipitation took place within, say, a week of June 18, 1946?

A. It would be impossible to say, without exact knowledge, just when that precipitation did occur. I have made up solutions of Vitamin B complex, trying to solve the precipitation problem and some of the experimental solutions [210] I made up I was feeling pretty good about

(Testimony of Roland N. Icke)

it, thinking that the problem had been solved. They stood in solution for sometime and then, on coming to work the next day, there was a precipitate in it. If I had not known the history of that in the meantime, I could not have said when that precipitation occurred.

The Court: What do you mean by "for some time?"

The Witness: A period of three or four days or a week.

The Court: Did you keep it in closed bottles?

The Witness: Yes.

Q. By Mr. Stick: Those experiments contained heavy doses of it? A. Yes.

Q. Is riboflavin itself soluble in water?

A. Very slightly.

Q. What are the bases in which it is dissolved?

A. I believe it has some solubility in alcohol, but I know that the presence of some other ingredients in a water solution will increase its solubility.

Q. Such as you have testified to? A. Yes.

Q. And in order to increase its solubility, some of these other substances are introduced? A. Yes.

Q. What factors affect the time in which a substance [211] of this type of solution will precipitate?

A. That is very difficult to say.

Q. Are there factors which could affect the precipitation such as you have in the bottles in Exhibit 1 after they were manufactured?

A. If the doctor had used any of that material and had carried out one of these injections where he had first used another material, so that he was mixing the two things, and had introduced some of the other material in here, by that he could have changed the nature of the

(Testimony of Roland N. Icke)

solvent, the material could have changed the nature of the solvent in which the riboflavin would dissolve.

Q. Under those conditions of temperature at which it was kept, would that affect the break-down of the substance or the precipitation?

A. It might, particularly if he had introduced any oxidizing materials or any substance which would increase the alkalinity.

Q. Have you made any tests of solutions similar to this which contained undissolved particles of pyrogen?

A. Yes. I tested a similar preparation containing undissolved particles injected into rabbits, and observed that their body temperature was not raised.

Q. Just describe to the court what you mean by pyrogen? [212]

A. The pyrogen test is prescribed by the U. S. P. as a means of determining whether or not a product is safe for injection.

Q. "Pyrogen" means what?

A. "Pyrogen" refers to the raising of the body temperature.

Q. Ordinarily spoken of as— A. Fever.

Q. —fever. All right. Then after you made this pyrogen test of this substance containing undissolved particles on the rabbits did you carry the experiment any farther?

A. Yes. I withdrew in a needle and a syringe some of the solution, observed it, and saw that there were particles suspended in the solution in the syringe, injected it into my own arm and observed no ill effects whatsoever.

(Testimony of Roland N. Icke)

The Court: This was a precipitate of riboflavin?

The Witness: Presumably it was riboflavin. That is the material which is generally considered as being what precipitates in all of these B complex solutions.

Mr. Stick: Might I have this bottle that has been referred to by the doctor, as containing four milligrams of riboflavin—may I have that marked for identification?

The Court: You may.

The Clerk: Do you want the box marked, too?

Mr. Stick: What? [213]

The Clerk: Do you want the box also marked?

Mr. Stick: I don't think that will be necessary; just the bottle.

The Clerk: This will be B for identification, Defendants'.

Q. By Mr. Stick: This product in the bottle marked Exhibit B, is that of the same general character as the things contained in Exhibits 1 and 2?

Mr. Neukom: Well, I don't like to object, but I think that is a matter the court ought to decide. It is obvious from my interpretation of the amounts there that it is not compounded similarly in amounts.

The Court: Overruled. He may answer.

A. That is also a Vitamin B complex preparation, as this says.

Q. By Mr. Stick: I believe you testified that it has some precipitate in it? A. Yes.

Q. Have you examined other similar Vitamin B products on the market as to whether or not they contain precipitates?

A. Yes. I purchased from Horton and Converse, and also from the Exclusive Prescription Pharmacy sev-

(Testimony of Roland N. Icke)

eral B Complex preparations put out by first-line pharmaceutical houses. I merely asked for a B Complex preparation and accepted whatever product they gave me.

Q. And that was true when you got Exhibit B? [214]

A. Yes.

Q. And did these preparations have precipitate in them? A. They did.

Q. And how much riboflavin was in these different bottles that you bought?

A. Well, varying amounts. I have one here that had only a half a milligram of riboflavin and it has precipitate in it.

The Court: Let that be marked for identification.

Mr. Stick: Yes, sir.

The Clerk: C for identification.

The Court: The bottle with the label on it?

The Clerk: Yes. The label says "Vitamin B Complex Parenteral 10 cc."

The Court: What was the riboflavin content?

The Witness: One-half milligram per cc.

Q. By Mr. Stick: You have shown one additional bottle, is that it? A. Yes.

Q. Is that the only other one you had?

A. No. I have others that I purchased at the same time.

Q. Do they contain precipitates?

A. Yes; they do. [215]

Q. They are B-1 solutions?

A. They are B Complex.

Q. B Complex solutions? A. Yes.

The Court: Do you wish them marked, Mr. Stick?

(Testimony of Roland N. Icke)

Mr. Stick: I think it would be well if they were. Will you describe each one of them and hand them to the clerk one at a time so that the clerk can mark them?

The Witness: This solution is called "VIJEX", V-i-j-e-x, produced by Galen Company, Inc., in Berkeley, contains per cc 10 milligrams of thiamine hydrochloride, $\frac{1}{2}$ milligram of riboflavin, 10 milligrams of niacin amide, 10 milligram of pyridoxine, 10 milligrams of pantothenic acid.

Mr. Stick: May that be marked D?

The Clerk: D for identification.

The Court: Do you have another one?

The Witness: Yes, sir.

The Court: The witness might describe it.

Mr. Stick: All right. Will you describe it?

The Witness: This is a product put out by Parke, Davis and Company. It says "Vitamin B Complex Parenteral."

Q. What does that mean?

A. It means that it can be injected. "Each cc. contains: Vitamin B₁ 10 milligrams, Vitamin B₂, or riboflavin, 2 milligrams, Vitamin B₆, or pyridoxine hydrochloride, 5 milligrams, nicotinamide, or niacinamide, 50 milligrams, [216] pantothenic acid (as the sodium salt) 10 milligrams." These substances also contain preservatives.

Q. Does this substance contain a precipitate?

A. I believe it does, a small amount.

The Court: Let that bottle be marked.

The Clerk: E for identification.

(Testimony of Roland N. Icke)

Q. By Mr. Stick: Now, in those bottles which you have introduced and said that you purchased at the pharmacy or pharmacies in the open market, and which contained the B-1 or B Complex solutions, and which you said had to some greater or less degree precipitate, can you tell from the examination of either of those when that precipitation occurred? A. Absolutely not.

Q. Did you ever make any test to determine whether that will go back into solution in any of these products?

A. Yes; on some materials I have tested and found that by warming them slightly the precipitate goes back into solution.

Q. That is in these B Complex? A. Yes.

Q. By the words "warming slightly" what would you mean?

A. Elevating the temperature above room temperature, but not up to boiling or anything like that.

Q. By how much would you say you would increase it over the amount that it had at the time that you started the [217] experimentation?

A. Probably would raise the temperature up to 50 or 60 degrees Centigrade.

Q. Which would be how much Fahrenheit?

A. That would be approximately in the range between 110 or 125 degrees Fahrenheit.

Q. And in some of those products which you have experimented with the matter would go back into solution from the precipitate? A. Yes.

The Court: In your opinion, would the precipitate in the two bottles comprising Exhibit 1, if they were placed in a pan of hot water?

(Testimony of Roland N. Icke)

The Witness: I believe it would. I would have to try it to be sure.

* * * * *

Q. You have before you now Exhibit 3, which is a bottle, and Exhibit 4, which is the label from that bottle, the label having on it the word "Indoform". Are you familiar [218] with that product?

A. Yes; I am.

Q. You see on that label the words "Thyroid Substance" 1 grain? A. Yes.

Q. Will you describe what would be meant by thyroid substance? A. With reference to this solution?

Q. Well, generally, and then with reference to that solution.

A. Thyroid substance, generally, or thyroid would refer probably to or would refer to dessicated thyroid powder which is generally given by mouth for treatment. An aqueous extract of thyroid substance would merely refer to that material which would be dissolved by water from the dessicated thyroid gland.

Q. Is there anything on that label which would indicate to a doctor whether that is a water-solution or extraction?

A. The very nature of the product itself, the fact that it is a glandular extract, would indicate to him that it is a water-solution.

Q. Would he, looking at that label, expect to find, normally, thyroxin in the solution?

A. Certainly not. [219]

(Testimony of Roland N. Icke)

Q. Why?

A. Because a doctor, if he wants thyroid activity, knows that for treatment he will give thyroid orally, that is by mouth. If he wants thyroid activity, he does not use an aqueous extract to obtain thyroxin, because thyroxin is not soluble in water. A great point of that is made in biochemistry, which every doctor is required to take, that the thyroid activity is almost unique in glandular hormone products, in that it is active by mouth. Many gland products are active only by injection, but thyroid is unique in being active by mouth; and that point is emphasized in biochemistry which every doctor takes.

Q. If there were no thyroxin—that is the part of the thyroid which contains the iodine—present would there be in an aqueous solution such as this a thyroid substance present?

A. Yes; there would be.

Q. And that is the substance that is referred to in the label?

A. Yes.

Q. Could you describe that substance?

A. To the best of my knowledge, there is no known chemical itself whereby it can be detected. I do know, though, that if thyroid substance or dessicated thyroid is extracted with water and the solution filtered so that you have a clear solution, that when that solution has evaporated there is a [220] residue, therefore, there is something dissolved.

Q. Would the Elmslee-Caldwell test for iodine disclose those substances which are in the aqueous solution?

A. That test is for organically combined iodine, and there is a test for thyroxin or other iodine-containing compounds characteristic of the thyroid gland. Since

(Testimony of Roland N. Icke)

this solution does not contain any thyroxin, you would expect to get a negative result. There would be no point in even assaying it for iodine.

Q. You will notice "posterior pituitary" is referred to on that label? A. Yes.

Q. Three international units. How is that extracted and put into that solution?

A. I have never extracted it myself. It is my understanding that it is also an aqueous extract. It certainly must be, in the fact that it appears in this aqueous solution.

Q. Are there any substances which will affect the thyroid substance that you have described, in the sense that it will destroy either the potency of the posterior pituitary or the thyroid substance? [221]

* * * * * * * *

A. I do not know of anything definitely in thyroid substance, as such, which might cause destruction of the posterior pituitary; but there are other ingredients in this same solution which might.

Q. By Mr. Stick: All right. What, for instance?

A. The suprarenal cortex, 30 grains. Suprarenal cortex extract, as prepared, almost invariably—I would say invariably—contains adrenalin or epinephrin; so that in a mixture of suprarenal cortex and posterior pituitary the mere presence of any adrenalin, although in this dose it would not be harmful to the human body, would repress any tests which were designed to show the presence of posterior pituitary. Adrenalin is an antagonist to a test as described by Mr. Mason.

(Testimony of Roland N. Icke)

The Court: What is this other substance you mentioned besides the adrenalin?

The Witness: Adrenalin was the one that I was referring [222] to.

The Court: Earlier, you say, "adrenalin" or some other substance.

The Witness: I know that from—

The Court: That it might contain.

The Witness: I know from experience.

The Court: No. I am just asking you that.

The Witness: Inherent.

The Court: You said that, due to this suprarenal cortex, that that substance might contain two substances, adrenalin and something else; and I did not understand the other substance.

The Witness: Adrenalin or epinephrin. "Adrenalin" is synonymous with "epinephrin".

The Court: And what is epinephrin?

The Witness: It is another name for the same thing.

The Court: For adrenalin?

The Witness: Yes.

Q. By Mr. Stick: Is adrenalin common in suprarenal cortex? A. Yes; it is.

Q. I understand, then, that what you mean is that the presence of suprarenal cortex in this solution would inhibit a test for or would interfere with the correct test for posterior pituitary as described by Mr. Mason? [223]

A. That is true.

Q. And would it show lesser or greater activity?

A. Since the effect of adrenalin is antagonistic or inhibitory to posterior pituitary, and posterior pituitary that was there would not be allowed to show its presence.

(Testimony of Roland N. Icke)

Q. So that the posterior pituitary under the circumstances would not, under that test, be as active as it would if the adrenalin was not present?

A. No; it would not. [224]

* * * * *

Mr. Stick: That is all.

Cross Examination

By Mr. Neukom:

Q. Dr. Icke? A. That is right.

Q. Doctor, there would be quite a dilemma if your theory is correct in the use of these items, wouldn't there? If he uses the alcohol or any sterilizing agent, he is going to ruin the efficacy of the product and take that chance?

A. Yes.

Q. If he does not use them, he is going to take a chance in giving his patient blood poisoning or some other infection, isn't he?

A. He could use some other sterilizing means or be careful that his syringes and needles were dry.

Q. When you made this product—well, incidentally, [227] right on that point, none of those four products here you had anything to do with their compounding, did you? A. No.

Q. The ones that are here in evidence, charged in this case? A. No.

Q. But you knew, and it is common knowledge, when these products were made that doctors did follow those means of sterilizing their needles, didn't they?

A. That had not been drawn to my attention until I had occasion to observe a bottle in which precipitation had occurred and that factor occurred as a possibility.

(Testimony of Roland N. Icke)

Q. Now, Dr. Icke, let us look at this Squibb product here, which is Defendants' B. And the bottle here, it is known as Parentosol. As a matter of fact the precipitation in that is so minuscule that you can hardly see it, isn't that true? A. It is hard to see.

Q. And let us look at the product that was put out by your employer, and the particles in there are large, some of them are?

A. Those could be very readily seen.

Q. The ones in the Exhibit B you can hardly see; isn't that true? [228]

* * * * *

A. Yes.

Q. This Exhibit 2 goes with Exhibit 1, the vial from Exhibit 1. Let's you and I compare the two component parts here, thiamine hydrochloride, from Exhibit 2; that label is 50 milligrams per cubic centimeter; isn't that right? A. That is right.

Q. Let us look here on Exhibit B; thiamine hydrochloride is only 10 milligrams; isn't that right?

A. That is right.

Q. All right. Riboflavin is 4 mgms. on the Squibb product, Exhibit B? A. Yes, sir.

Q. And it is 2 on your product?

A. That is correct.

Q. Now, nicotinamide. A. Niacinamide.

Q. Niacinamide, which you state helps dissolve the riboflavin; isn't that correct?

A. It is one of the things that helps.

Q. That is the same material as on Exhibit 2 called "nicotinamide"? A. Nicotinamide.

(Testimony of Roland N. Icke)

Q. Spelled a little differently here, but it is the same product, isn't it? [229]

A. There are two names that are used: Niacinamide or nicotinamide. They are the same.

* * * * *

Q. And these two names are here from Exhibits B and 2? A. Yes, sir.

Q. Let us notice the great difference. There are 200 milligrams to four milligrams of riboflavin, whereas in your product there are only 50 milligrams to 2; or, in other words, it is four times as much, isn't it?

* * * * *

A. That is true.

Q. And you state that that nicotinamide has a tendency to dissolve the riboflavin?

A. It assists the solution; yes.

Q. It assists. Then, in your opinion, this is a better combination, if you expect to have undissolved particles, isn't it?

A. Not necessarily, because of the other substances also in solution.

Q. Would you, Doctor, be surprised if it were true that this Government's Exhibit 1, one of these vials, has [230] been placed in a very warm, almost boiling, bowl of water and still these particles did not dissolve?

A. I would expect them to dissolve.

Q. Doctor, have you noticed on Exhibit B that you brought here, in which we can virtually see if there are any particles there, do you note that it says right on here with the package: "If crystals of riboflavin form,

(Testimony of Roland N. Icke)

they may be dissolved by immersing the vial in lukewarm water.”? A. Yes.

Q. Do you note anything like that on Government’s Exhibit 2? A. No.

The Court: You are referring to the box which contains Exhibit B for identification?

Mr. Neukom: Yes, your Honor.

* * * * * * * *

The Court: Is there objection, Mr. Stick, to marking the box in which it came a part of Exhibit B for identification?

Mr. Stick: No, your Honor.

Mr. Neukom: Incidentally, may it be so marked?

I note the Squibb bottle has, in addition to the rubber stopper that you can see, there is a metal stopper, too? [231] A. Yes.

Q. Which has to be taken off before it can be utilized, is that correct? A. That is correct.

Q. That has been on the market for some time, hasn’t it? A. I have seen it on several products.

Q. However, the trade has found that these rubber caps in the fashion that your firm uses and other firms use is quite acceptable, haven’t they? A. Yes.

Q. And, as a matter of fact, Doctor, this testimony that you have given with respect to doctors introducing, for instance, with the Vitamin B material, the thiamine hydrochloride, introducing some oxidizing agent, or as a result from this alcohol that you mention, or from the mercury substance or any of these other sterilizing agents, that is upon the assumption, is it not, Doctor, that that

(Testimony of Roland N. Icke)

has actually been introduced into the vial and has caused a deterioration; isn't that true? A. Yes.

Q. And had not such an agent been introduced, and if it be true that no air had gotten in, why, you would not expect any deterioration in any of these products containing either the Vitamin D or the Vitamin B-1, the thiamine [232] chloride, would you?

A. If it had been kept under normal conditions, I would not.

Q. What would you assume to be above normal conditions on B-1 as far as temperatures are concerned?

A. That would be a relative matter.

Q. Well, what would be in your opinion above?

A. I would say that any temperature above 100 to 120 degrees Fahrenheit might be above what you would consider normal.

Q. If the bottle was sealed as in that bottle, would you expect it to deteriorate within a matter of a few months down to only 33½ per cent?

A. If that bottle had been setting in the sunlight so that the temperature got up high, or any other factor which might have elevated the temperature, it might have deteriorated.

Q. Let us assume that the bottle had been kept in normal temperature. It has been your practice and observation of most doctors that they try to keep their bottles in proper places, has it not, Doctor?

A. I believe most of them do; yes.

Q. And it is rare that you find a doctor but what he adheres to the cautions that he has been instructed; isn't that correct? [233] A. Yes.

(Testimony of Roland N. Icke)

Q. You would assume, would you not, Doctor, that had this bottle not been opened and another agency placed into it that would have caused its deterioration that you speak of, that you should expect, in three or four months or even longer, that that substance would remain stable, wouldn't you? A. Yes.

Q. You would be rather surprised to find it was short about 30 per cent, would you not, or 33 1-3 per cent?

A. Yes.

* * * * * * * *

Q. By Mr. Neukom: Doctor, what is there on this label here, this Indoform label, that shows that this is an aqueous solution?

A. The fact that it is an extract of glands.

Q. I am referring to Government's Exhibit 4, the first count. Now, do you not put up extracts of glands in a soluble solution and in an aqueous solution and expect some therapeutic value from it?

A. Some glands; yes. [234]

Q. Well, wouldn't you put up a thyroid substance in that manner and expect any therapeutic value?

A. Certainly not.

Q. Then, in other words, when thyroid is placed in a solution it has no value of a therapeutic nature whatsoever?

A. It has no thyroid activity that is known. That does not mean that it does not have any value.

Q. Well, what do you mean by that?

A. I mean that if a doctor wanted to use a product for the thyroid value, he would give thyroids in a solid form by mouth. He would not—

(Testimony of Roland N. Icke)

Q. Doctor, haven't you heard of many, many people taking injections of glandular substances containing thyroid by intravenous or intramuscular?

A. They are for other conditions besides thyroid disorders normally.

Q. What are they for?

A. I am not familiar with the exact use, but I do know that if a doctor wants thyroid—the benefit of thyroid, he gives it by mouth and not by injection.

Q. But you will concede, Doctor, that you know that there are solutions given intravenously or intramuscularly of thyroid substances which are taken for a specific purpose, is that right? [235]

A. I don't know how—

The Court: Do you mean by that, for the purpose of thyroid relief?

Mr. Neukom: Yes; some therapeutic value from thyroid.

A. Not for the therapeutic value of thyroid, I would not say.

Q. Aren't there extracts of glands, thyroid glands, which are made up in water solvents?

A. Yes.

Q. Do you know of any other thing in which they dissolve thyroid substance into?

A. No.

Q. Do they dissolve it into alcohol?

A. I don't know. An alcohol solution probably would not be injectable.

Q. Do you know of any published work or anything that you have read, Doctor, which indicates that a water-soluble extract of thyroid has any physiological effect?

A. No.

(Testimony of Roland N. Icke)

Q. Are we to understand that this, then, this product here, the thyroid substance, was a nullity; it really meant nothing?

A. To the best of my knowledge, there is no therapeutic value from an aqueous extract of thyroid substance.

Q. Doctor, you have stated that this adrenalin that [236] was present in this—I can't remember these terms.

The Court: Suprarenal cortex.

Q. By Mr. Neukom: —suprarenal cortex has a tendency to make it impossible, or it sort of works against the discerning of the presence of posterior pituitary, is that correct? A. That is correct.

Q. Do you mean by that that it makes the posterior pituitary less efficacious? I am referring now to Government's Exhibit 4.

A. No; I don't mean that it makes it less efficacious.

Q. Well, do you mean that the analysts can't find and could not hope to find posterior pituitary because of its presence?

A. It would depend upon the relative amounts of adrenalin and posterior pituitary whether you could detect the presence of either one of them in the test.

Q. Oh. In other words, there isn't any assurance here as to the amount, then, of adrenalin that is present in Government's Exhibit 4?

A. I know of no assay to determine quantitatively that amount that is present there in that sample.

Q. Well, then, you just assume that this suprarenal cortex does contain adrenalin which might be enough to make you unable to determine whether or not there was

(Testimony of Roland N. Icke)

posterior [237] pituitary present in the amounts as indicated on that label?

A. I have assayed solutions which were made by extraction of suprarenal cortex and other glandular materials and have found adrenalin present.

Q. Well, let us take this one right here; that is the one we are interested in. Would you say that the suprarenal cortex of 30 grains per each cubic centimeter—is it your testimony that that is a sufficient amount and contains a sufficient amount of adrenalin that you can't hope to find posterior pituitary when you analyze that and follow the tests that have been testified to here by Mr. Mason?

A. I would have to analyze it for the adrenalin in order to be able to answer that question.

Q. Well, in other words, you were just surmising when you said that a while ago; you have no specific knowledge on whether or not that suprarenal cortex does contain an amount sufficient to eradicate the hope to discover the posterior pituitary?

A. I know that it takes only a small amount of adrenalin to counteract the effect.

Q. Vedy well. Take Defendants' Exhibit No. D, the Vijex product and, Doctor, make a fair comparison of that product with a portion of vial No. 1, from the vial, Exhibit No. 1; isn't it true that the fragments, if any, in D are almost undiscernable? [238]

A. Yes; they are hard to see. [239]

* * * * *

Mr. Stick: I would like to ask that the exhibits we introduced for identification yesterday—I believe it is B, C, D, and E—be now admitted into evidence.

(Testimony of Roland N. Icke)

Mr. Neukom: No objection.

* * * * *

The Court: Defendant's Exhibits for identification A, B, C, D, and E are now received into evidence.

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By Mr. Neukom:

Q. Dr. Icke, I was inquiring of you with respect to what is the subject matter of Count VII, the undissolved particles in the vial, a part of Government's Exhibit No. 1; [241] and you had produced certain other vials such as B, C, and D, the products, and we had discussed them, asked questions and answers had been given with regard to those. I believe it was your statement that, in your opinion, these undissolved particles should dissolve in warm water or in lukewarm water, is that correct?

A. I would assume that they would.

Q. Would that be in water, say, around about 110-120 degrees Fahrenheit? A. I would guess so.

Q. Well, is that your opinion? A. Yes.

Q. Then, if Government Exhibit No. 1, the vial, does contain undissolved particles of riboflavin, that is the Pluri-B—no; it is the Pluri-B product which had two milligrams in it—it is your view that the riboflavin was not fully dissolved, is that correct?

A. I didn't say that.

Q. Well, then what is correct on that?

A. You are referring to the exhibit?

Q. I am referring to Exhibit 1, the vial, and then the label, which is Government's Exhibit 2, the Pluri-B

(Testimony of Roland N. Icke)

which had two milligrams, whereas the other Pluri-B had one milligram.

A. It is my opinion that something has happened to [242] the solution so that the riboflavin is no longer dissolved.

Q. I see. Doctor, do you know how that solution is prepared? A. In a general way.

Q. Just explain.

A. I know that the different ingredients are dissolved in water. This particular solution I am not certain the order in which the ingredients are dissolved. I know that they are finally all in the same solution and are dissolved by warming.

Q. Well, they are all put into one glass basin and mixed, and then ultimately put into a large bottle—or would that be the correct procedure—and then, later, drawn off into the individual vials?

A. That would be the general idea.

Q. I see. When we have a condition of precipitation such as in Government's Exhibit No. 1, we have what is called supersaturated solution, do we not, of the riboflavin?

A. In the present condition of this bottle, I would say that that probably is correct.

Q. Well, if it was fully saturated, it would be dissolved; that would be correct, wouldn't it? When anything is supersaturated in the tenor of your terms, it is because the aqueous solution or the solvent is not able to dissolve the particles; isn't that correct? [243]

A. That is correct with reference to the particular condition of the solution at the time when that condition exists.

(Testimony of Roland N. Icke)

Q. I see. Now, Doctor, is it not your opinion that if this product was made and left to stand a period of time of overnight, and it had too much riboflavin in it, that within a short period of time that would show up, wouldn't it? A. Yes.

Q. And if a person was being careful and cautious when preparing the sterile solution such as this for intravenous or intramuscular use, they should, by experimentation, seek to ascertain when the other solvents or water or medicaments are ample to dissolve the riboflavin, shouldn't they?

A. Yes; that is the purpose of inspection.

Q. And that would not be very difficult, would it?

A. No.

Q. And if a manufacturer would but wait a short while and allow his solution to stand, he would readily detect that this condition was existing and could correct it, could he not? A. I believe so.

Q. Now, Doctor, yesterday we were discussing your views with regard to the possible existence of adrenalin in the suprarenal cortex of the solution known as Indoform, which is Government's Exhibit No. 4, the label is. Will you [244] please tell the court what gland the adrenalin gland is and where it is located?

A. The label on the bottle speaks of "suprarenal cortex extract", as I remember.

Q. Suprarenal cortex 30 grains, I believe, in each.

A. The suprarenal gland is also called the adrenal gland and is located near the kidney, generally.

(Testimony of Roland N. Icke)

Q. The adrenal gland and the suprarenal gland are the same?

A. The adrenal and the suprarenal, they are two names for the same gland.

Q. For the same gland. Do you know what term or word the "adrenal" comes from?

A. It would only be by surmise. It is my understanding that the word "renal" refers to kidney, and "adrenal" would be near the kidney.

Q. The gland, is it not divided up into two parts?

A. That is true.

Q. And what are the two parts?

A. The cortex and the medulla.

Q. And the medulla is the part of the gland from which the adrenalin comes; isn't that correct?

A. It originates in the medulla.

Q. And the cortex itself is not the gland which contains that substance, is that right? [245]

A. It is impossible to remove all of the medullary substance from the cortex; so that suprarenal cortex always contains some of the medulla and, therefore, always contains adrenalin.

Q. Now, you were here when Mr. Bavouset testified as to how he prepared the Indoform in question here. As I recall he stated that, with regard to the thyroid substance in this product reflected by Government's Exhibit No. 4, he mixed them up in a water solution and shook it to some extent; in fact, I think he said a day elapsed before he mixed it with the other products; isn't that correct, or do you have a recollection of that?

A. I do not recall exactly.

(Testimony of Roland N. Icke)

Q. Well, do you know if that is the way it was prepared?

A. I don't know the time intervals. I have never made any of the combination.

Q. Are you acquainted with how the suprarenal cortex is dissolved or is added to this compound?

A. Only that it is dissolved in water; I know that.

Q. And is it not, of course, exposed to air and to oxidation in so doing?

A. The extracts that I have seen made have been in bottles that were stoppered.

Q. In the process of packing it, of course, it is [246] exposed to the air, is it not? A. To some extent.

Q. And is it not true that the very small amount of adrenalin that might be in the suprarenal cortex, if the suprarenal cortex substance is pure, as established by the United States Pharmacopoeia, is rapidly deteriorated by air and oxidation?

A. It is my understanding that the Pharmacopoeia states that there is a certain percentage of adrenalin in U. S. P. suprarenal cortex. That is my recollection. And I know that on assays of finished preparations of this type I have found adrenalin in solution.

Q. Haven't you also found that adrenalin also acts as a contracting agent as applied to the uterus, or have you ever performed the test?

A. I do not recall that fact.

Q. You do not know whether it does, then, or it does not?

A. I know that in general, as far as I know it,—well, I would say practically always, as far as I know,

(Testimony of Roland N. Icke)

it always causes a relaxation on smooth muscles which are used for testing its activity.

Q. Doesn't it also contract muscles?

A. I don't know.

Q. You don't know. Well, what makes you say that [247] adrenalin negatives the effect of posterior pituitary?

A. Because posterior pituitary will contract smooth muscle and adrenalin will relax smooth muscle; so that there is an antagonistic effect.

Q. That is true if you have adrenalin in some large amount, rather than in the amount which is very insignificant in a pure product of suprarenal cortex; isn't that true?

A. I have a reprint, if I may draw it to your attention, in which only one millionth of the mol of adrenalin causes a relaxation of small muscle.

Q. Do you wish to refer to either one of these books?

A. All right.

Q. Your counsel has handed me these, and I don't know where.

A. On pages 137, 138, and 139 of this reprint I have circled some micrograph tracings showing the effect of a tenth of a minus six molal of epinephrin, 10 to the minus 6 meaning one-millionth of a mol.

Q. Does this test also embody the usage of posterior pituitary? A. It does not.

Q. Well, that is adrenalin, then, of itself, isn't that right? A. Yes.

Q. Have you ever performed a test on a uterus en- [248] deavoring to ascertain whether or not posterior pituitary in combination with a pure substance of

(Testimony of Roland N. Icke)

~~(cerebral)~~

suprarenal cortex would retard or restrict a test such as Mr. Mason testified to here?

* * * * *

A. Not on posterior pituitary itself, I haven't; but I have observed a test on other agents which also cause contraction of the smooth muscle and have observed the inhibiting effect of adrenalin on the contraction. And I know that the presence of adrenalin in combination with a material which, by itself, would cause contraction inhibits that contraction so that you will not get the full extent of the contraction which this other substance, by itself, would show.

It is my opinion that I have graph 1-B in which pure posterior pituitary in water and diluted acetic acid, as Mr. Mason described it was tested, that if he had also put some adrenalin with that, he would have got a smaller con- [249] traction; that curve would not be extended as high and, with proper amounts of epinaphrin, he might have gotten no contraction at all, and with further amounts, he might even have received an acute relaxation.

Q. How much adrenalin do you think was present in the suprarenal cortex involved here?

A. I don't know. I didn't assay that solution.

Q. What smooth muscle do you refer to when you state that you have noted that adrenalin relaxes it?

A. I know it does on certain of the viscera of animals, such as the large and small intestine, which is a smooth muscle of the same general shape that the uterus is. I know that it will do that with rabbits or guinea pigs. There apparently is no species difference.

(Testimony of Roland N. Icke)

Q. Adrenalin is also used a great deal for heart conditions, is it not? A. Yes.

Q. And then it comes in a form whereby the product definitely states that it is adrenalin, doesn't it?

A. I believe so.

Q. You would not expect to buy adrenalin for a heart condition where it was labeled "suprarenal cortex," would you? A. No.

Q. In fact you would not be even looking for any adrenalin if the designation was "suprarenal cortex," would [250] you?

A. It is inherent in the preparation of suprarenal cortex that there will be adrenalin with it.

Q. Do you happen to know where a product such as—aren't these things such as whole ovarian and posterior pituitary and a product such as this Indoform—do you happen to know what that is used for? Is that not used for women for some of their troubles?

A. I don't know definitely what use it has. I just know that the doctors ask for it; so apparently there must be some value. And I know that there has been no advertising and no attempt to sell it in the laboratory, other than just to act like a pharmacist in fulfilling the doctors' orders.

Q. I see. Doctor, yesterday you were testifying that Vitamin B-1 or thiamine hydrochloride does deteriorate under certain adverse conditions such as excessive heat; isn't that correct? A. Yes.

Q. And will deteriorate so to what extent?

A. If I may refer to some notes that I have?

Q. Under what?

(Testimony of Roland N. Icke)

The Witness: I would like to refer to some notes.

The Court: You may. If it is necessary, you may step down and get them.

The Witness: Thank you. [251]

A. The extent to which Vitamin B-1 deteriorates with heat depends both upon the temperature and the pH. I have—

Q. May we assume or will you tell me whether the pH. in Pluri-B—well, refering to Government's Exhibit 7—whether or not in your opinion was not the pH. proper in that instance when it was manufactured?

A. Yes.

Q. And then if that continued on without the introduction of any foreign substance into that vial, the cap was not removed, in your opinion pH. should have continued below 7, shouldn't it?

A. If there were nothing else to interfere; yes.

Q. Light would not affect it, would it, the pH.?

A. I would not expect it to. I don't know of any.

Q. And normal heat would not affect it, would it, room temperature and such as that—the pH. I mean?

A. I would not expect it to.

Q. All right. Now, what, then, is destructive of this Vitamin B-1, this thiamine hydrochloride?

A. Anything which might have been introduced into the bottle in the course of use.

Q. Well, these means that you testified about yesterday, about the alcohol or the sulfites or air that might have gotten in from puncturing the rubber cap, is that correct? A. Yes. [253]

(Testimony of Roland N. Icke)

Q. But if that did not occur, you would not expect a deterioration of the B-1, would you?

A. I would expect the B-1 to retain its potency if there were no external reasons.

Q. You would not expect within a few months for it to lose its potency up to 30 per cent, would you?

A. No; under normal conditions.

Q. And you heard Chemist Capps' testimony and, I think, subscribed to his views that the test that he gave to ascertain the quantity of B-1 was the approved test, did you not?

A. He was the one that described the dark room test, was he?

Q. Yes; I think it was fluoroscopic, was it not? Thiachrome test. I was not acquainted with the term.

A. The thiachrome.

Q. Thiachrome. Thiachrome, and they went through some color arrangement. Thiachrome tests, yes.

A. I believe that when the thiachrome test is carried out properly that it is a fair measure for Vitamin B-1 potency.

Q. I would like to call to your attention—you are acquainted with the Supplement to the Twelfth Edition of the Pharmacopoeia, a little bound booklet which I have here, are you not? [254]

A. To some extent.

Q. You know that this is a standard work, is it not?

A. Yes.

Q. And is an authority and is well accepted among your field and the medical field and among druggists, is it not?

A. It is regularly accepted.

(Testimony of Roland N. Icke)

Q. Read with me. You note that I am reading from pages 82, 83:

“Thiachrome assay for thiamine hydrochloride.”

That is for B-1, is it? A. Yes.

Q. Let us read down here at the bottom:

“After preparation of assay solution, the amount of material taken for the assay should be such that the ratio of the volume of tenth normal sulphuric acid used for the extractive amount of sample is at least 15 to 1 and the content of thiamin equivalent to 30 to 100 micrograms of thiamine hydrochloride.”

Now, I want you to note this next sentence:

“Place the accurately-weighed quantity of material to be assayed in 65 cc's of tenth normal sulphuric acid contained in 100 cc's centrifuge tube and digest it in a steam bath with frequent mixings for 30 minutes.” Do you note that? [255] A. Yes.

Q. It says, “for 30 minutes” that that thiamine hydrochloride is to be placed on a steam bath. Does that not mean that activated hot steam is actually flowing up against the tube in which that is and reaches almost a boiling point?

A. That is true. But the pH. of that strong sulphuric acid would be down around 1. The lower edge is an extremely low pH. and you would not expect the thiamin to be not stable at a very low pH.

Q. Isn't the product in here such to keep at around 3, didn't you say on your opening testimony?

A. Yes.

(Testimony of Roland N. Icke)

Q. And that is rather low and one that you would expect to stay stable, too, as compared to 7, isn't it?

A. Yes; but it would be less stable than it would at a pH. of 1.

Q. But I ask you if that steam would not almost constitute a boiling condition; isn't that correct?

A. Yes.

Q. And that also states to keep it on that for 30 minutes, doesn't it? A. Yes.

Q. And while that process is going on the product is subjected to oxidation from air getting in about it; isn't [256] that true?

A. I would like to see that again, please?

Q. Well, you do not enclose the product while the steam is flowing upon it and you are assaying it, do you? The part that I have marked here at the bottom. (Referring to book.)

A. This was done in a centrifuge tube, so apparently it was open to the air.

Q. And that is a more adverse condition, with a revolving or with a full allowance of air, than occurs in a vial of the character of one of these, is it not?

A. I do not believe that that is revolving during that time.

Q. Well, at least, these do keep out air, do they not, these vials? A. Yes.

Q. Such as the one I have in my hand?

A. Yes.

Q. So, then, you would expect the Vitamin B content or the thiamine hydrochloride to stand up in a closed vial after six months, and retain the potency or practically the potency that was reflected from the label, if

(Testimony of Roland N. Icke)

it did have that amount when the label was placed on it, would you not?

A. I would if nothing else had affected it.

Q. Now, I would like to ask you something. Epinephrin [257] is another word for adrenalin, is it not?

A. Epinephrin.

Q. Epinephrin. And you are acquainted with the work, a Manual of Pharmacology by Solomon, are you not?

A. Yes.

Q. And the Fifth Edition, is that correct?

A. Yes.

Q. And it is a recognized authority in its field, is it not?

A. Yes.

Q. A standard work, I mean. Is it correct that whenever I use the word "epinephrin" that I could also be using the word "adrenalin"?

A. That is correct.

* * * * *

Q. "Reversal of adrenalin"—while the word here is "epinephrin"—"inhibition by pituitary extract. The uteri of guinea pigs and non-pregnant rats are ordinarily relaxed by epinephrin or adrenalin." That is what you stated just a while ago?

A. Yes.

Q. "If, however, they are first treated with pituitary [258] solution, the epinephrin or adrenalin produces contraction." Do you subscribe to that?

A. Yes.

Q. "The difference in the normal resistance of different uteri to epinephrin may, therefore, depend on the content of pituitary. This sensitizing action seems to be in the

(Testimony of Roland N. Icke)

peripheral nervous mechanism and not in the muscle itself." Do you subscribe to that statement or doctrine?

A. That is correct; but I believe you have brought out the wrong implication.

* * * * *

Mr. Stick: Pardon me, please, your Honor.

Mr. Neukom: I beg pardon.

Mr. Stick: I think he wanted to make an explanation of that answer.

The Court: He may.

A. This says: "If, however, they are first treated with pituitary solution, the epinephrin produces contraction." It does not say that if they are simultaneously treated with posterior pituitary and epinephrin, that contraction will take place.

Q. By Mr. Neukom: Didn't you hear Chemist Mason state that that is just what he did? He treated this [259] substance with pituitary first.

A. But he did not add epinephrin to it.

Q. But you say epinephrin was present in this suprarenal cortex.

A. There is quite a difference there. After his test 1-B, that test smooth muscle was washed so as to remove all of the posterior pituitary. That is shown by the fact that the record of the contraction came back to normal; so that there was no posterior pituitary there, and that it was in a condition the same as if no posterior pituitary had been added at all. That is further verified by the fact that the record of 3-B is essentially that of 1-B.

Q. Doctor, didn't you state that this amount of adrenalin or epinephrin in the suprarenal cortex, while

(Testimony of Roland N. Icke)

you did not know whether it was there or not, it could be in such a small amount it would still have an effect? Now, would the washing remove even that small quantity also? A. Yes.

Q. In other words, it would be present to retard this test, according to your opinion, upon your surmise that it is present in suprarenal cortex, is that it?

A. I know it is present in suprarenal cortex.

Q. But yet the label says nothing about its presence; isn't that correct? A. That is correct. [260]

Q. Doctor, is it not true that the public today buy bread with Vitamin B-1 placed in it and that the enriched flour, so enriched, retains its potency even after the baking of the bread?

A. That is true, but there is a difference between a solution and the material in the relatively dry form. A solution is more susceptible to change than the dry material.

Q. Don't they have to mix that up and heat it up with the dough in order to form the bread?

A. Yes.

* * * * * * * *

Q. And it has to be dissolved; it is not just a mere powder in there, is it? A. No.

Q. Doctor, isn't it likewise true that your cereals which are placed in ovens, they have added B-1 or thiamine hydrochloride to them and they come out and they are potent?

A. They are potent, but I know that an excess is added above the amount claimed for that product, because the manufacturers expect a certain amount of loss.

(Testimony of Roland N. Icke)

Q. You really, actually, Doctor, feel that this Pluri-B product that your employer puts out is a pretty stable product; it is not a fragile product, is it?

A. It is intended to be stable. [261]

Q. And you would be highly surprised if within a few months after its manufacture, it was 30 per cent off, wouldn't you?

A. If nothing had happened to it, I would be surprised.

Mr. Neukom: That is all.

Mr. Stick: That is all.

The Court: I have two or three questions of the doctor. Doctor, taking up, first, this Vitamin D (in oil).

The Witness: Yes, sir.

The Court: What would have to happen to that solution to reduce the potency from a half million units per cubic centimeter of Vitamin B down to 350,000, in your opinion?

The Witness: In my opinion, some oxidizing agent would have to have been added to that for the potency to decrease.

The Court: Can you illustrate to what extent an oxidizing agent would have to be introduced into the solution and how it might be done? Would it have to be done intentionally?

The Witness: No; it would not have to be done intentionally.

The Court: Could it be done by use of the doctor in perforating the rubber cork with a hypodermic needle containing a sterilizing solution such as you referred to yesterday?

(Testimony of Roland N. Icke)

The Witness: Yes; it could very readily be done that way without the doctor's realizing that it was being done.

The Court: Well, would one such injection of a hypo- [262] dermic needle carry it out or would it require, likely, repeated use?

The Witness: It would only take one to cause some destruction. It would be impossible to say without knowing just how much of the oxidizing agent was added and at what temperatures the materials were kept.

The Court: Suppose the doctor did, as I believe you described, puts his needle in some alcohol and shakes it off and squirts it out, and puts the needle into the rubber cork, would such a process as that likely introduce an oxidizing agent that would reduce the potency of the contents of the bottle by several thousand units?

The Witness. It would reduce the potency some. I have no way of knowing just how much it would reduce it.

The Court: But if you assume that here was a product, Vitamin D (in oil), manufactured with a potency of 500,000 units of Vitamin D per cubic centimeter, and six months later, say, was found to have only 350,000; if you assume that, if the only use had been made of it had been the injection of the doctor's hypodermic for the purpose of extracting the solution from the bottle, would you assume that there had been many such applications of the hypodermic?

The Witness: Probably so.

The Court: And would you assume there had been extremely careless use, shall I say, by the doctor? [263]

The Witness: No; I do not believe I would call it careless. So far as I know, it has not been called to

(Testimony of Roland N. Icke)

the doctors' attention that there are oxidizing agents in isopropyl alcohol.

The Court: Assume if the doctor picked up his hypodermic and puts it in isopropyl alcohol, and supposing he tries to be real careful and shakes it and manipulates the needle two or three times, the syringe part of it, in an attempt to clear the container of any foreign substance at all, and then wipes it off, he can't wipe out the interior of the needle, can he?

The Witness: No; nor the syringe.

The Court: Yes. So if he injects that, inserts it through the rubber cork, he is likely, in your opinion, greatly to decrease the potency of the next injection?

The Witness: I believe it is quite possible and very likely that it would reduce the potency.

The Court: Considerably?

The Witness: Yes.

The Court: How many hypodermic injections in the normal use of Vitamin D for such a purpose could be expected from this bottle which is Exhibit A?

The Witness: Is that a 30 cc vial?

The Court: I am sure I can't tell you. It is not labeled, I think. Would you like to examine it closer?

Mr. Clerk, will you hand it to the witness? [264]

The Witness: This is a 15 cc vial.

The Court: Approximately how many hypodermic injections could a doctor procure of Vitamin D from that vial?

The Witness: From 15 to 30.

The Court: From 15 to 30. The patient who might be No. 28, in your opinion, would likely get a practically useless injection, wouldn't he?

(Testimony of Roland N. Icke)

The Witness: The amounts of material which he would undoubtedly put into the bottle would vary considerable with how many times he moved the plunger back and just how dry the needle and syringe became by that process; so that it would be extremely variable.

The Court: Yes; I understand. But I am assuming the normal process that we have been describing, of a doctor who tries to be careful but who cannot be so meticulous as to bake his hypodermic dry each time before he inserts the needle into the solution.

The Witness: The last doses would be considerably less potent than the first.

* * * * *

The Court: I want to turn now to this one or two counts with respect to Pluri-B. Pluri-B for intramuscular use con- [265] tains, according to the label, one milligram of riboflavin. Is that, in your opinion, coupled with the other ingredients, sufficient for the purpose for which Pluri-B is intended?

The Witness: The opinion of the medical doctor who uses that varies considerably. Some of the doctors want even more riboflavin and some others, less. It is a matter of their own opinion. I would not be qualified to say.

The Court: I am asking your opinion, not the doctor's opinion.

The Witness: I see.

The Court: In your opinion, this product, Pluri-B, containing one milligram of riboflavin is sufficient for the purpose for which it was intended?

The Witness: Yes.

(Testimony of Roland N. Icke)

The Court: And it is marked "for intramuscular use." It is sufficiently potent, in your opinion, with respect to riboflavin, is that correct?

The Witness: Yes, sir.

The Court: Can you tell me why the same product, Pluri-B, which is intended not only for intramuscular, but also for intravenous use, contains two milligrams, twice the amount?

The Witness: I know that some of the other manufacturers have prepared more concentrated solutions, that is, solutions containing more riboflavin; and that the laboratory had received requests for B Complex solutions which had more [266] riboflavin in it than the one milligram.

The Court: What I am getting at, do you know of any reason why the stronger solution should be marked for intravenous as well as intramuscular use, whereas the solution that is intended for intramuscular use only is the weaker solution insofar as riboflavin is concerned?

The Witness: I do not believe that the riboflavin content there would make any difference whether it would be used intravenously or intramuscularly.

The Court: Would it be erroneous to assume that a solution that has one milligram per cubic centimeter of riboflavin, that the riboflavin in such a solution would be less likely to precipitate than a similar solution or a like solution containing twice as much riboflavin per cubic centimeter?

The Witness: If the other ingredients in there were the same, it probably would be less likely to precipitate.

The Court: That is our assumption, is it not?

The Witness: Yes.

(Testimony of Roland N. Icke)

The Court: The Pluri-B that we are referring to is identical, except that the one marked for intramuscular or intravenous use has twice as much riboflavin as the solution which is marked for intramuscular injection only.

The Witness: Yes.

The Court: That is all I have. [267]

Mr. Neukom: I just wanted to ask, since you brought up a subject.

Q. Doctor, if a needle is sterilized in a steam cabinet, there would therefore be removed any oxidizing agent, would there not?

A. I suppose so. If the oxidizing agent is water-soluble, I think that would be removed.

Q. Now, Doctor, don't you know—you have talked about oxidizing agents here and you have told the court where you think they may come from. Is it true, Doctor, that this sterilization process of the little baths, the very chambers that the doctors have will actually sterilize the needle and leave no oxidation agent on the needle?

A. Not all oxidizing agents are water-soluble. I don't know about the oxidizing agent in isopropyl alcohol, whether it is soluble or not; so I could not say whether the steam treatment would remove it.

Q. Now, Doctor, most medical men have this little needle which fits onto a sort of a glass tube, that they can see how much they are drawing in, don't they, from the plunger? A. Yes; they observe the solution.

Q. Isn't it true that about 80 to 90 per cent of the physicians have that needle removed and that needle is placed in a boiling bath of water, thoroughly sterilized before it is used to obtain any of these solutions to inject into people; [268] isn't that true?

(Testimony of Roland N. Icke)

A. I know that a great many doctors do. I don't know what the percentage is. I know some of them do not use that process; they use isopropyl alcohol or mercuricides almost exclusively.

Q. If the doctor did use the first process, the sterilization process, you would not believe that there should be any oxidizing agent to any extent that you have stated might affect the product, do you?

A. If he had not previously used a material in which some water-insoluble oxidizing agent had got on the material, I would agree with you.

Q. What if he had previously used isopropyl alcohol and then steamed and sterilized his instrument; would you state that that alcohol would still remain there in an amount of sufficient oxidizing agent to affect this Vitamin B?

A. It is not the alcohol that is an oxidizing agent. The peroxides are dissolved in the alcohol, and I don't know whether the peroxides are soluble in water or not; so I couldn't say whether they would be removed.

Q. Doctor, you have never actually performed tests where you have taken a hypodermic needle, stuck it in some alcohol, shook it dry, allowed the volatile alcohol to go off, then insert it in one of these bottles, draw out repeatedly, and then determined how much potency had been [269] lost as a result of, say, 10 or 12 such tests?

A. No.

* * * * *

The Court: That is all, Doctor.

Mr. Stick: Defendants rest.

Mr. Neukom: I would recall Dr. Tolle just for a few more questions, your Honor.

PLAINTIFF'S CASE IN REBUTTAL

CHESTER D. TOLLE,

recalled as a witness in rebuttal by plaintiff, being previously sworn, was examined and testified as follows:

Direct Examination

By Mr. Neukom: [270]

* * * * *

Q. Before going on that, you were in charge of the office for a certain branch of the files in the office of the Food and Drug, were you not?

A. I received all samples.

Q. And you had occasion to receive this sample that Chemist Capps—I have allowed him to go, your Honor—you had occasion to first receive that, did you not?

A. I did.

Q. And that is Government's Exhibit 7, I believe—Government's Exhibit 6, the Pluri-B. When that was received in this vial that has been testified to here, did you have occasion to observe whether or not that vial when received appeared to be full and appeared to be not tampered with? A. It did.

Q. Appeared to be in the state of a new vial, is that correct? A. That is correct.

Q. And you passed it on to the other analyst after analysis? A. That is correct. [271]

Cross Examination

By Mr. Stick:

Q. Dr. Tolle, have you ever run any experiments at all [272] with reference to tests of an oxidizing agent

(Testimony of Chester D. Tolle)

getting into a bottle containing Vitamin D by the use of a hypodermic needle?

A. No; because that has not been of interest to me.

Q. You have not run any tests and have no knowledge from the experience of a test on that point?

A. You are quite right. I would like to explain my answer, if I may.

The Court: You may.

A. In the case of the products that we examine, we do not have occasion to examine bottles that have been opened, because I see all the records as they come in with the sample and, had a sample been opened the record would so indicate and then we would not make a test on it in our laboratory. That is one thing that is an unwritten law with the inspectors, according to my opinion and according to advice I have heard given to them, that they make known whether or not a sample that has been picked up has been taken out of the container.

Q. By Mr. Stick: Now, you say they make that known. How do they make that known?

A. By a note on the collection record.

Q. And that note says that they have not opened it?

A. No; it does not say that they haven't opened it.

Q. What does it say?

A. If it has been opened, it so states; and then they [273] have an affidavit from the doctor or the pharmacist or whoever may have indicated that he has opened it.

Mr. Stick: Your Honor, there being no testimony before of such thing in either of these instances, any surmise on his part would be purely hearsay as to a test, that it had been opened.

(Testimony of Chester D. Tolle)

The Court: That is a matter of argument. He has merely said in effect that the inspector is to report that he has been informed that this bottle had not been opened.

Q. By Mr. Stick: Did you ever see any of these bottles before they arrived in your hands in Washington on some particular day that you have testified to?

A. I did not.

Q. You do not know, of your own knowledge, when they were shipped? A. I do not.

Q. Or, of your own knowledge, to whom they were shipped? A. I do not.

Q. Or, to your own knowledge, what happened to them when they were received by the consignee of the shipment? A. Certainly not.

Q. Of your own knowledge, you have no knowledge as to what was in the bottles at the time they were shipped? A. No.

Q. All you know about it is that at the time it came to [274] you in Washington it appeared to be an unopened bottle and one that had not been used?

A. That is right.

Mr. Stick: That is all.

Redirect Examination

By Mr. Neukom:

Q. You do know what you found from your analysis?

A. That is right.

Q. And you have heretofore testified to that?

A. I have.

Mr. Neukom: That is all. [275]

* * * * *

Mr. Neukom: Mr. Mason.

ARNOLD E. MASON,

recalled as a witness in rebuttal by the plaintiff, having been previously sworn, was examined and testified as follows:

Direct Examination

By Mr. Neukom:

Q. With respect to the vial designated as 3 which you, and then, later, Mr. Buell analyzed and which is in [276] support of Count I, will you tell the court the condition of the contents of that vial and the apparent condition of the sealer or cork when you first received it in conjunction with your duties?

A. The vial was full and the rubber stopper or cork was protected, with a celluloid seal around it when I received it. It appeared as if it had never been opened.

Q. Will you just tell the court once more with regard to this subject matter, now, of adrenalin or epinephrin? Will you tell the court just what you did with regard to first washing the uterus horn with the pituitary standard solution?

A. The uterine horn is allowed to relax to a constant level before the assay is ever begun, then a standard solution of posterior pituitary is added to that bath, the muscle is caused to contract by that pituitary solution. When it contracts to a maximum for the given amount of standard pituitary given to it, the bath is washed out and clean, fresh, aerated bathing fluid is again surrounding the muscle. The muscle relaxes to its normal level again and that procedure is either repeated or an amount of sample is added to the bath.

The Court: In this case, after you washed out, shall I say, the bath from the first test with the standard

(Testimony of Arnold E. Mason)

solution, you applied to it the solution under investigation?

The Witness: The solution under investigation was then added in 2-B on the board. [277]

* * * * *

Q. Mr. Mason, are you acquainted with the properties of the adrenalin gland?

A. Yes. I have performed assays on adrenalin solutions for the Food and Drug Administration for over three years.

Q. And the adrenalin gland is composed of two parts, is it?

A. It is composed of the adrenal medulla and cortex.

Q. And does the cortex itself contain adrenalin?

A. The cortex might contain very small amounts of adrenalin. The main hormone of the cortex is its own hormone.

Q. From your experience and from your studies do you have an opinion as to whether or not suprarenal cortex, 30 grains, as is indicated on this product here, Indoform, contains sufficient adrenalin to make it impossible to test posterior pituitary that you were testing for in this test?

A. That would depend upon what form the suprarenal cortex was in and under what conditions it was put into solution and upon how much adrenalin was present originally in the gland—in the cortex of the gland. [278]

(Testimony of Arnold E. Mason)

Q. In this particular instance here what is your opinion, bearing in mind what you have testified to, to explain now as to the existence or lack of existence of posterior pituitary in those products mentioned?

* * * * *

A. As I have stated before, there is little or no posterior pituitary in that product from the results of my test.

Q. Do you think your test was equally as effective or non-effective by the fact that this product had in it suprarenal cortex or will you explain?

A. I believe the test was as effective as if suprarenal cortex had not been there. I have had occasion to assay many other preparations of similar nature, glandular preparations, and the amount of posterior pituitary that is claimed can be assayed for and proved to be present in the presence of other glandular preparations and suprarenal cortex.

Q. In the presence of suprarenal cortex? Is that correct?

A. Yes, sir.

Mr. Neukom: That is all.

The Court: Do you agree that the presence of a quantity [279] of adrenalin or epinephrin in the suprarenal cortex, constant in the liquid, would tend to negative the test you made for the presence of posterior pituitary in the solution?

The Witness: No, your Honor; I do not. Under the conditions of this test the bath in which the guinea pig uterus is suspended is being constantly aerated with oxygen. It is commonly known that adrenalin is very unstable in air, and also that adrenalin is very short

(Testimony of Arnold E. Mason)

acting, that is, it will act for a short time, because it is dissipated both by the tissue and by air oxidation. Posterior pituitary, on the other hand, is quite a long acting drug. I think, first, that the adrenalin, if it was present, would have been destroyed so rapidly that it would not have interfered with the test.

The Court: Would the treatment of the uterine muscle with the standard solution of posterior pituitary which you made in the first test, would that carry over after the bathing of the muscle preparatory to the second test, so as to prevent the presence of any adrenalin from interfering, or would the bath negative the first application of posterior pituitary for that purpose? I am referring now to the text which was read here to Dr. Icke, in which the author stated, as I recall it, in substance, that the treatment of the muscle with posterior pituitary would prevent the interference by the epinephrin or adrenalin.

The Witness: I don't know what the author of the text [280] means by pre-treating with posterior pituitary. If he means he adds pituitary preparation to a uterine muscle and lets that pituitary stay in solution, then adds the adrenalin, he must be very careful of the amount of pituitary that he adds, in order to prove his point; for if he is not, the muscle will contract to a maximum and he will never be able to say that adrenalin would enhance the pituitary contraction or it would reverse itself and cause a contraction. It seems to me that he must have pre-treated the muscle in a manner such as this, then washed the solution out and immediately added epinephrin.

The Court: In other words, washed the muscle just as you did upon the completion of the first test?

(Testimony of Arnold E. Mason)

The Witness: Yes. There is a great species difference, as can be cited in the literature, in the action of adrenalin on uterine muscles—not only on smooth muscles, but even on uterine muscles. It will act different in different species; and just exactly what the author means in his text I can only surmise; and that is, that he does not mean that he keeps the pituitary in the solution and adds the adrenalin on top of it.

The Court: If you assumed that, by reason of the presence of suprarenal cortex in this solution of Indoform which you were testing, some epinephrin or adrenalin was present, would you feel that you should make some allowance for that fact [281] in your conclusions?

The Witness: Do you mean in this test?

The Court: Yes.

The Witness: Under the conditions under which I was running tests, I would not feel I should make any allowance unless that fact was so stated on the label.

The Court: Irrespective of what the label said, if we assume—I am asking you to assume, now?

The Witness: Assume that adrenalin—

The Court: That it was present by reason of the presence of the suprarenal cortex in that solution; and if you so assume, would that alter your conclusions as to the accuracy of your test?

The Witness: Not as to the accuracy of my test.

The Court: Would it alter your conclusion which you have stated as to the presence or absence of posterior pituitary in that solution?

The Witness: No, sir. I am sorry I misunderstood your question in the first place.

The Court: That is all I have.

(Testimony of Arnold E. Mason)

Mr. Neukom: I might ask him this one question, your Honor:

Q. Does the viscera and the uterine muscle all react the same with the same stimulus?

A. No, sir. [282]

Q. Explain.

A. As I explained a moment ago, there is a difference in the way viscera and uteri will act in different animals. There is even a difference in the way the uterine muscle itself will act in different animals. For example, adrenalin may contract the uteri of some animals; it may relax the uteri of other animals. There is no hard and set rule. It depends upon the animal. The only way that that can be proven is by investigation. The only way the action of a drug can be shown is by investigation.

The Court: What animal did you use the uterus of here?

The Witness: A guinea pig.

The Court: What is the effect of adrenalin upon the uterus of the guinea pig?

The Witness: In normal guinea pigs, adrenalin by itself will relax the muscle.

The Court: This was a normal guinea pig that you used?

The Witness: A guinea pig prescribed in the test.

The Court: So you would assume, would you, that if the adrenalin was present in the solution, that the tendency of that adrenalin as present would be to relax the muscle, and hence to counteract the tendency to contract?

(Testimony of Arnold E. Mason)

The Witness: Not if pituitary solution was also present. [283]

* * * * *

The Court: By that, do you mean that the presence of pituitary would tend to negative the presence of the adrenalin, and vice versa?

The Witness: You are assuming that adrenalin is present in this solution?

The Court: Yes. I have not assumed any quantity.

The Witness: It would depend both upon the quantity of both adrenalin and pituitary.

The Court: Yes. So if there were an "X" quantity of adrenalin, it might be a stand-off so far as the effect on the muscle is concerned with "Y" quantity of pituitary, is that correct?

The Witness: Do you mean with an amount of adrenalin present in that solution might inhibit any action of the pituitary?

The Court: Inhibit the action of the muscle, might it not?

The Witness: To pituitary?

The Court: In other words, if there is a quantity of adrenalin in the solution which, as I understand it, you would say in a normal situation would tend to relax that muscle?

The Witness: Yes, sir. [284]

The Court: Here is an unknown quantity of posterior pituitary which, as I understand it, would tend to contract the muscle?

The Witness: That is right.

(Testimony of Arnold E. Mason)

The Court: If that adrenalin were present, before you could measure the presence of posterior pituitary by the muscular contraction, there would have to be enough to overcome whatever counter-effect the adrenalin would have, would there not?

The Witness: It would have to be enough. But, according to the text that was read in court a while ago, in the presence of pituitary the epinephrin relaxation would be reversed.

The Court: You mean by that, is it your understanding that the presence of adrenalin or epinephrin and pituitary in the same solution would convert the epinephrin into a contracting agent on the muscles instead of a relaxing agent?

The Witness: I would assume that that is what would happen.

The Court: That is all I have.

Mr. Neukom: May the witness just read that paragraph, your Honor? He was not present or close when this was being read, and he might want to make an explanation. I will not read it into the record here.

Q. After having read that, do you wish to make any [285] additional explanation to the court to clarify your position?

A. No. I again state that I think that the adrenalin in this sample under investigation, if it was present, definitely would not have interfered with any assay for posterior pituitary.

The Court: Why do you say that? Why would that be so?

The Witness: I have examined a number of other samples, as I have stated, glandular substances very simi-

(Testimony of Arnold E. Mason)

lar in nature to the one under investigation. I have examined them for labeled contents of posterior pituitary. There are other similar samples which claim three international units per cubic centimeter of posterior pituitary on the label, also containing these other glandular constituents. And they can be assayed and it can be shown that the amount of posterior pituitary present is 100 per cent of the labeled potency.

The Court: Irrespective of the presence—

The Witness: Irrespective of the presence of suprarenal cortex. I will not say “adrenalin”, since we are assuming that adrenalin is in this product. We have no proof of it.

The Court: So, irrespective of the presence of adrenalin?

The Witness: Irrespective of the presence or absence of adrenalin, those assays were still carried out and it was shown that the labeled content of posterior pituitary was [286] present.

The Court: Doesn't that make a question; there might have been more than three, might there not, in that solution that you are referring to? Now, might there not have been enough posterior pituitary, first, to overcome whatever counter-effect or relaxing effect the adrenalin present might have had, plus the three units?

The Witness: The assay showed the presence of only three units per cubic centimeter.

The Court: Yes. But the assay was the same type of assay you made here?

The Witness: Yes, sir.

The Court: And might there not have been, in order for you to reach that result—

(Testimony of Arnold E. Mason)

The Witness: More than that?

The Court: There was three units plus enough neutralizing counter-effect of the quantity of epinephrin present?

The Witness: If any excess was present— I don't believe I can answer that question.

The Court: How can you know, if you start out with the supposition that the presence of epinephrin would tend to neutralize the pituitary present, how could you ever know how much pituitary was present unless you did something about the adrenalin that might be present?

The Witness: The only way you could know how much was [287] present, as I said, is to assay it.

The Court: I am only interested in the end result here. Our problem is to determine whether this pituitary is present; and if so, in what quantity. Isn't that our problem?

The Witness: Yes. The only way that could be determined is by an assay for the presence of posterior pituitary.

The Court: It could not be determined by the test you made?

The Witness: That test I made is not what one might call an assay, because it is impossible to get an assay with the product under investigation. In the official United States Pharmacopoeia there is an assay for posterior pituitary which starts in this manner. However, the sample being investigated must cause a contraction of the muscle as great as the standard solution when one is given following the other for four doses, then a fifth dose of standard solution must be given, which is 25 per cent higher than the other two doses of the

(Testimony of Arnold E. Mason)

standard solution, to show that the muscle has not been contracting at a maximum all that time; in other words, that it could have gone higher if it wanted to; that the preparation under investigation was not actually 150 per cent of what you were testing it for, but that the contraction went up only as high as the standard and, if given in amounts equivalent to that of the standard solution, it therefore would have the same strength of the standard, and [288] if that was made up according to the labeled potency, it would be 100 per cent.

The Court: Have you made any test to determine the relative quantity of epinephrin present in a given amount of suprarenal cortex?

The Witness: No, sir.

The Court: That is all I have.

Q. By Mr. Neukom: Do you know whether epinephrin does, though, rapidly oxidize and pass away under tests such as you have made?

A. Very rapidly. It is rapidly oxidized in the air, and in a test like this, as I stated, there is oxygen bubbling through the bath to aerate the muscle, and that oxygen present would rapidly destroy minute amounts of adrenalin.

The Court: Would you assume that there would be minute amounts where the quantity of suprarenal cortex present is 30 grains per cubic centimeter?

The Witness: Very minute amounts, if any.

The Court: How would you know that?

The Witness: The only way you could know whether any amount of adrenalin was present would be to test the preparation for adrenalin. [289]

* * * * *

Mr. Neukom: Dr. Wiley for just a couple of questions, if your Honor pleases.

FRANK H. WILEY

called as a witness in rebuttal by plaintiff, having been previously sworn, was examined and testified as follows:

Direct Examination

By Mr. Neukom:

Q. Dr. Wiley, when you received Government's Exhibit No. 1 there was in all how many vials?

A. Six vials.

Q. And of the two that have been produced here, did they appear to be sealed, capped and full?

A. They did. All six of the vials, as a matter of fact, were full. [290]

* * * * *

Q. By Mr. Neukom: Did all six of the vials appear to have a percentage of undissolved particles such as the one that is a part of Government's Exhibit No. 1?

A. They did.

Q. Did you endeavor to pass these vials into a lukewarm bath to ascertain whether or not the dissolved particles would become saturated?

A. I did. That is a part of the general routine in examining products of this type in the laboratory. We first examine the product while the label is still on the vial, if that is at all possible. Sometimes the label covers up so much of the vial that it is almost impossible to see the contents. But where we can see them on any portion of them, we examine the material for undissolved particles. Then, to make a more complete inspection, the vials are placed in warm water which runs around 150

(Testimony of Frank H. Wiley)

degrees Fahrenheit and are allowed to remain in there for a period of time of about 10 to 15 minutes. During that time the labels are loosened from the vials and float off. The vials are then dried and the contents re-examined.

In this particular case the undissolved material was still present although the solution in these vials was quite warm. [291]

Q. While this was not a matter that you testified to, I forgot to ask it of Dr. Tolle. Is it not true that thiamine hydrochloride or the B-1's and the complexes are, in addition to being a food, also in a classification of a drug?

A. Yes; they are so classed. The fact that thiamine hydrochloride appears in the U. S. Pharmacopoeia makes it a drug under the Food and Drug and Cosmetic Act.

Mr. Neukom: That is all.

The Court: In picking up these samples does the Administration pay the person who has the samples for them?

The Witness: We always offer to make payment. Sometimes that is not required, but ordinarily it is required and we make whatever payment is necessary for the samples.

* * * * *

Mr. Neukom: The Government rests now, your Honor.

The Court: Do both sides rest?

Mr. Stick: Yes, your Honor. [292]

* * * * *

Arguments were made on behalf of the parties and the matter submitted to the Court.

* * * * *

The Court: The court finds the defendants guilty as charged in Count I of the Information; and guilty as charged in Count II; guilty as charged in Count III; guilty as charged in Count IV; not guilty as charged in Count V; not guilty as charged in Count VI; and guilty as charged in Count VII of the Information.

Guilty as to all counts other than V and VI, and not guilty as to Counts V and VI. [342]

[Endorsed]: Filed Aug. 11, 1947. [343]

[Endorsed]: No. 11690. United States Circuit Court of Appeals for the Ninth Circuit. Pasadena Research Laboratories, Inc., a corporation, and Russell R. Bavouset, Appellants, vs. United States of America, Appellee. Transcript of Record. Upon Appeals From the District Court of the United States for the Southern District of California, Central Division.

Filed August 23, 1947.

PAUL P. O'BRIEN,
Clerk of the United States Circuit Court of Appeals for
the Ninth Circuit.

In the United States Circuit Court of Appeals
for the Ninth Circuit

No. 11,690

PASADENA RESEARCH LABORATORIES, INC.,
a corporation, and RUSSELL R. BAVOUSET, an
individual,

Appellants,

vs.

UNITED STATES OF AMERICA,

Appellee.

STATEMENT OF POINTS WHICH APPELLANTS
INTEND TO RELY ON THE APPEAL, PUR-
SUANT TO RULE 19(6) OF THIS COURT

On appeal, Defendants-Appellants intend to rely on the
following points in support of their appeal:

I.

The District Court erred in overruling defendants' ob-
jection to the latter of the following questions propounded
to the witness Wiley:

"Q. By Mr. Neukom: Dr. Wiley, taking the
two vials, part of Government's Exhibit No. 1, which
I understand you examined about six weeks after
the shipment in question here, from your knowledge
of sterile solutions and from your observation of
sterile solutions, your experience, are you able to
express an opinion to this court as to whether or
not the contents of those two vials, Government's
Exhibit 1, did contain the undissolved particles you
noticed there then as of the date they were shipped,

namely, on or about June 18, 1946? Your answer is yes or no."

* * * * *

"Q. By Mr. Neukom: Will you please relate your opinion?" (Reporter's Transcript of Proceedings, page 17, lines 9 to 18, and page 18, lines 17 and 18.)

II.

The District Court erred in overruling defendants' objections to the following questions put to the witness Mason:

"Q. Assuming, Mr. Mason, that this product was not exposed to excessive temperatures, that is to say, that you said was 212 degrees is the destructive temperature; and assuming the product was handled in a normal and careful manner, retained in the bottle, as Government's Exhibit No. 4, I believe; assuming which bottle you opened and conducted the tests as you have testified; and, with the assumption of what you found or did not find at that time, have you an opinion as to whether or not this product contained three international units of posterior pituitary on September 17, 1945?"

* * * * *

"Q. By Mr. Neukom: Now assuming that all that you have testified to here and the explanations you have given, what is your opinion, carrying on the assumptions that I have enumerated—what is your opinion as to the amount, if any, of posterior pituitary was in the product on or about September 17, 1945?" (Reporter's Transcript of Proceedings, page 61, lines 16 to 25, and page 62, lines 6 to 10.)

III.

The District Court erred in overruling defendants' objections to the following questions put to the witness Capps:

"Q. Now, assuming that the product received ordinary and reasonable care, and was not exposed to excessive heats, such as heats any more than would be normal from shipping and the weather, and basing upon what you found on September 24, 1945, the amount of the B-1 or thiamine chloride that you found, have you an opinion as to what percentage or what amount that product, substance, or solution had on or about July 16, 1945, the date it was originally shipped?" (Reporter's Transcript of Proceedings, page 94, lines 12 to 19.)

IV.

The District Court erred in that there is no evidence in this case upon which a finding of guilty could be made against either of the defendants.

V.

The District Court erred in that the finding of guilty is contrary to law.

VI.

The District Court erred in that the finding of guilty is contrary to the weight of the evidence.

VII.

The District Court erred in that the finding of guilty is not supported by substantial evidence.

VIII.

The District Court erred in that it did not give defendants the benefit of reasonable doubt which they were legally entitled to.

IX.

The District Court erred in that the evidence in this case did not demonstrate beyond a reasonable doubt the defendants' guilt.

X.

The District Court erred in that the Government failed to eliminate the possibility of the products having lost their strength or potency through the failure or neglect of parties other than the defendants.

XI.

The District Court erred in that the Government failed to prove that heat, or light, or lack of refrigeration, or moisture did not in some way come in contact with the bottles so as to cause the alleged loss of strength.

X.

The District Court erred in entering judgment in favor of the United States, while, in fact, and law, it should have been entered in favor of the defendants.

Dated at Los Angeles, California, this 15 day of September, 1947.

JOHN C. STICK

R. WELTON WHANN

By R. Welton Whann

Attorneys for Appellants

Received copy of the within Statement this 15 day of Sept., 1947. James Carter, by N. W. Neukom, Attorney for Appellee.

[Endorsed]: Filed Sep. 18, 1947. Paul P. O'Brien, Clerk.

No. 11690

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

PASADENA RESEARCH LABORATORIES, INC., a corporation,
and RUSSELL R. BAVOuset,

Appellants,

vs.

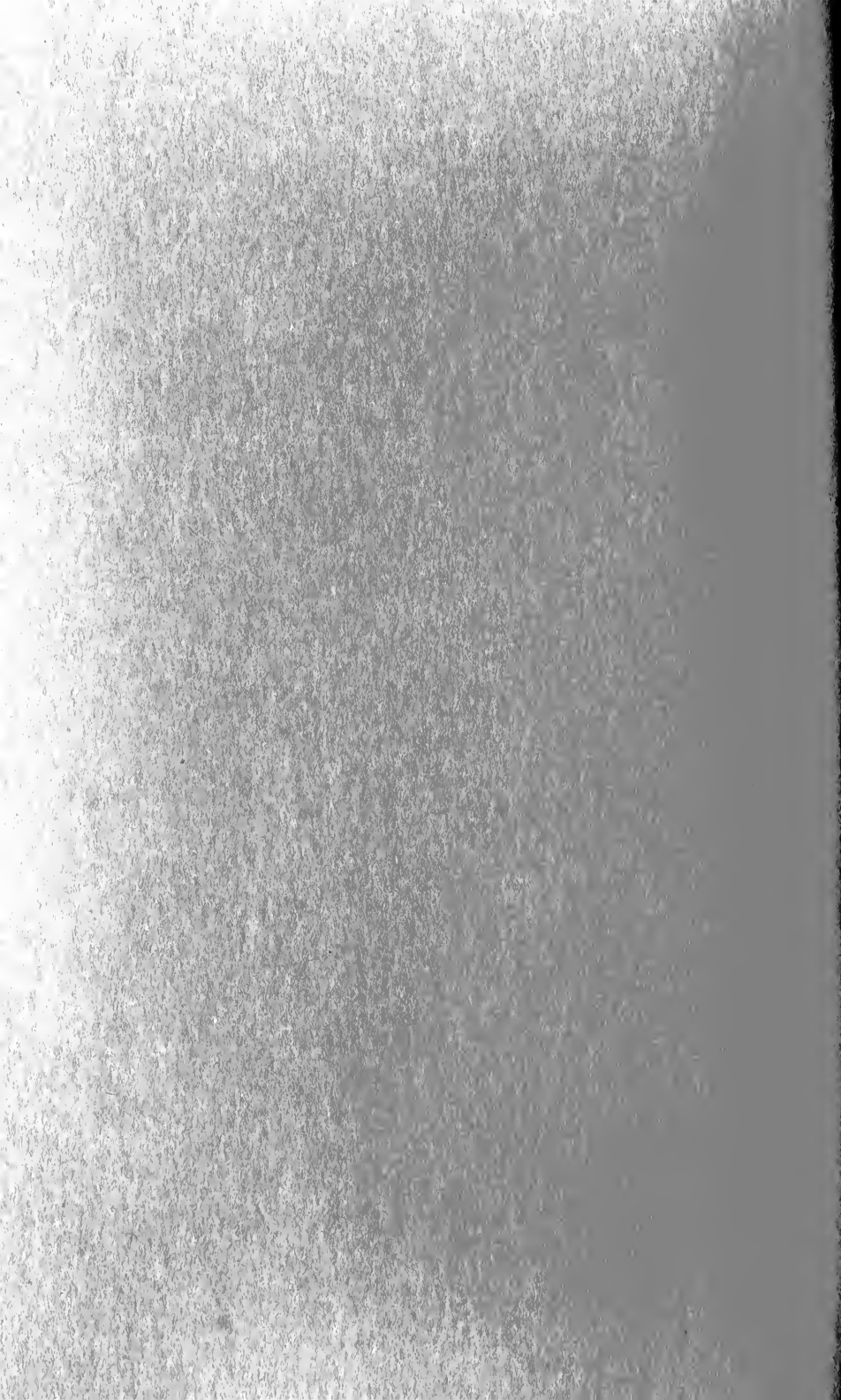
UNITED STATES OF AMERICA,

Appellee.

APPELLANTS' BRIEF.

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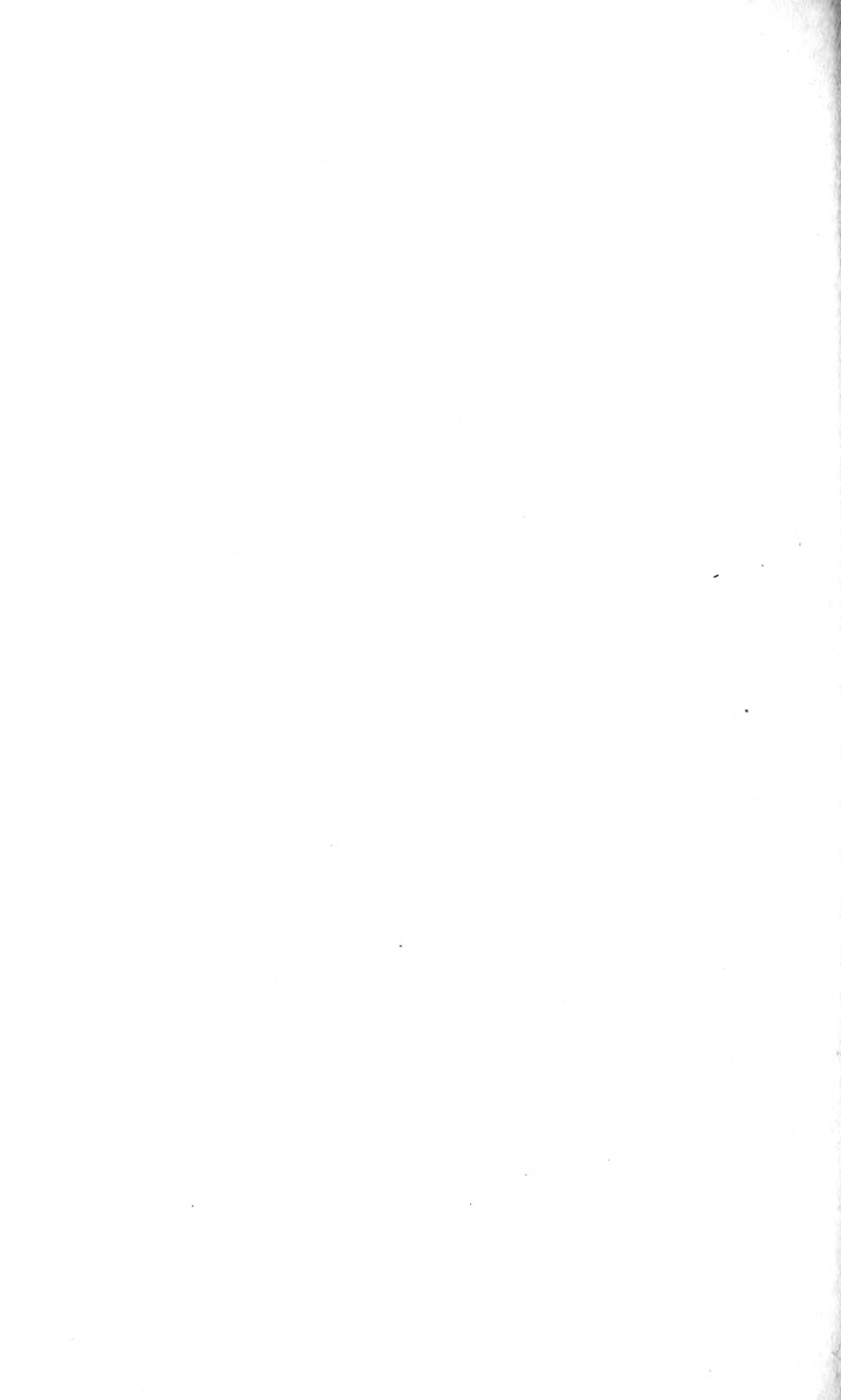
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No. 11690

IN THE

United States Circuit Court of Appeals
FOR THE NINTH CIRCUIT

PASADENA RESEARCH LABORATORIES, INC., a corporation,
and RUSSELL R. BAVOuset,

Appellants,

vs.

UNITED STATES OF AMERICA,

Appellee.

APPELLANTS' BRIEF.

Statement of Pleadings and Facts Re Jurisdiction.

The United States Government on March 18, 1947, filed an Information [R. 2] containing Counts I to VII in which both appellants were charged with "violation of the Federal Food, Drug and Cosmetic Act" (21 U. S. C. A. 331 and 333) in that they "did * * * unlawfully cause to be introduced and delivered for introduction into interstate commerce" drugs which were then and there adulterated and misbranded. Both appellants were found guilty on Counts I to IV inclusive and Count VII, and not guilty on Counts V and VI. Even though this was the first alleged offense of either appellant, the corporate appellant was fined \$3,000.00 and the individual appellant Bavouset was placed on five years' probation [See Judgment R. 20 and Probationary Order R. 22, filed July 7, 1947].

Within the statutory period, and on July 16, 1947, both appellants filed their notices of appeal [R. 24, 25].

No jurisdictional questions arose in the Lower Court and it is believed that no jurisdictional questions will arise in this Court, this Court having authority to review the District Court's decision under 28 U. S. C. A. 225(a) and (d).

Concise Statement of Case.

Counts I and II, III and IV, and VII, each involve separate sets of facts which are briefly stated as follows:

Counts I and II, Indoform, Exs. 3 and 4.

As stipulated [R. 14], vials or bottles, Exs. 3 and 4, containing the product "Indoform" were shipped in interstate commerce on or about September 17, 1945, from Pasadena, California, to Dr. Joseph C. Bunten, Cheyenne, Wyoming. This vial was picked up on or about January 24, 1946, by Government inspector Ralph M. Davidson and was mailed to the Food and Drug Administration, Washington, D. C.

The Government contends that each cubic centimeter of this product did not contain three International Units of posterior pituitary, and that each cubic centimeter of this product did not contain 1 grain of thyroid substance, as set forth on the label, Ex. 4, on September 17, 1945, when it was introduced into interstate commerce.

On February 18, 1946, the contents of the vial, Ex. 3, were examined, and Arnold E. Mason, a pharmacologist and analyst of the Food and Drug Administration, Washington, D. C., testified that the tests he made showed practically no posterior pituitary in the product [R. 59].

The sole evidence introduced by the Government as to whether or not this product contained the amount of

posterior pituitary set forth on the label, Ex. 4, on September 17, 1945, the date it was introduced or delivered into interstate commerce, is an *opinion* expressed by Government's witness Mason in response to an *improper* hypothetical question, duly objected to, and which question included facts not proved and which question was based on the assumed existence of facts, the existence of which was not established by any evidence whatever in the case.

The Government introduced no evidence whatsoever to establish that physical changes did not occur in the goods after it was shipped by appellants; whether or not it was properly cared for; whether or not it had been exposed to excessive light; whether or not it had been protected from undue temperature variations; whether or not it had been tampered with; or whether it had been added to or otherwise adulterated by anyone between the time the goods left appellants' place of business and was introduced in interstate commerce, and the time the tests were made by Government witnesses.

The Government *erroneously* argues that the term "Thyroid Substance" on the label, Ex. 4, means that the product contains iodine; and that the product is misbranded and adulterated because the witness Buell, a chemist for the Food and Drug Administration at San Francisco, on March 27, 1946 [R. 85] tested the product for its organically combined iodine content [R. 87] and found none present [R. 89].

The Government witness Buell did not test this product for any "thyroid substance" other than iodine [R. 96]. He admitted, however, there could be other parts of the thyroid gland in solution [R. 94].

Appellants rebutted these contentions by the positive testimony of the appellant Bavouset, who testified of his own personal knowledge as to the compounding of the product and that the product contained three International Units of posterior pituitary and one grain of thyroid substance [R. 110]. The appellant Bavouset is a chemist and has had about twenty years experience in the pharmaceutical business [R. 108] and has been making Indoform, the product under discussion now, for about fifteen years [R. 109].

The evidence on behalf of the two appellants is that the label does not state that iodine is present; they freely admit that there never was any iodine in the solution; and that the Government and its witnesses are unwarranted in contending that iodine is represented to be present in the solution [R. 111].

The label, Ex. 4, specifies thyroid substance which is not the drug in the United States Pharmacopoeia known as "thyroid". The official definition of thyroid is "Thyroid is the cleaned, dried and powdered thyroid gland previously deprived of connective tissue and fat" [R. 136].

A disclaimer was put on the product stating that it did not contain therapeutically useful constituents, to definitely let the doctor know that the thyroid content was not the iodine content [R. 111]. The Government witness Buell admitted that the label indicated that there was no active substance of thyroid in the solution [R. 95].

Counts III and IV, Pluri-B, Exs. 6 and 7.

As stipulated [R. 15], the vial and label, Exs. 6 and 7, were shipped by appellants on July 16, 1945, to Dr. Clement Swaim, Reno, Nevada. The Government inspector Griebeling picked up two vials and contents on

August 30, 1945, and shipped them to Food and Drug Administration, Washington, D. C.

The Government witness Capps on September 24, 1945 [R. 97] examined the contents of Ex. 6 and found that it contained thirty-three milligrams of thiamine hydrochloride instead of fifty milligrams, as stated on the label, Ex. 7 [R. 100].

This witness was then asked the improper hypothetical question in which it was assumed “* * * that the product received ordinary and reasonable care, and was not exposed to excessive heats, such as heats any more than would be normal from shipping and the weather, * * *” none of which assumed facts are supported by any evidence whatever in the case [R. 100]. In response to said improper question Capps gave his opinion that on September 24, 1945, when shipped, the contents did not contain more than thirty-three milligrams of thiamine hydrochloride per cubic centimeter [R. 100, 101]. Thus the only evidence supporting the Government’s case is the *opinion* of the Government witness Capps, based on an *improper* hypothetical question containing facts not proved.

As in the case of Counts I and II, there was no evidence whatsoever to prove that physical changes did not occur in the product *after* the date of shipment by appellants, or as to what happened to the product or with regard to the conditions to which it was exposed from the time it was shipped by appellants until tested by the Government, or as to whether or not the goods had been tampered with. The Government witness Capps testified that he did not make any examination of the cap of Ex. 6 to determine whether it had been punctured [R. 106]; in other words, tampered with.

Bavouset testified that thiamine hydrochloride will deteriorate if subjected to light or heat, if exposed to air over a period of time, etc. [R. 115, 149]. Dr. Icke also testified as to its instability under certain conditions [R. 159].

The appellant Bavouset testified with regard to Counts III and IV and particularly with regard to Exs. 6 and 7; that the contents were probably made by himself [R. 114]; that all of the materials set forth in the label were combined in the solution, and at the time the solution had the full strength and potency set forth on the label [R. 115].

Count VII, Pluri-B, Exs. 1 and 2.

As stipulated [R. 16, 17] a number of vials with labels, of which Exs. 1 and 2 are exemplary, were shipped by appellants on June 18, 1946, to Dr. P. M. Ryerson, Phoenix, Arizona. The Government inspector Kerr collected six vials and contents on or about July 12, 1946, and shipped them to Food and Drug Administration, Washington, D. C.

The Government witness Wiley received the samples, Ex. 1, on July 23, 1946 [R. 33], and upon inspection found that they were badly contaminated with undissolved material [R. 34]. The Government witness Wiley was then asked the *improper* hypothetical question, duly objected to, and in answer to which he gave his *opinion* that the “* * * undissolved material was undoubtedly present on June 18th when the material was shipped * * *” [R. 42].

The hypothetical question was bad and improper because it did not include a sufficient factual basis to support an opinion in that no mention whatever was made

of the conditions to which the drug had been subjected after shipment by appellants. Furthermore, even if the question was proper Wiley's opinion given in response thereto is not entitled to any weight whatever.

Wiley admitted that temperatures slightly above freezing would cause the material in solution to precipitate. As in the case of all of the other counts, there was no evidence whatever as to what happened to the product or with regard to the conditions of light, temperature, etc., under which it was kept from the time it was shipped by appellants from Pasadena, California, until tested by the Government's witness Wiley in Washington, D. C.

Bavouset testified that the precipitation might be due to fluctuation of temperature [R. 145]. Dr. Icke testified that the precipitation might have been due to conditions of temperature, or the addition of other substances into the vial [R. 171, 172].

There is no evidence that these particles do not constitute material which *was added* to the vials after the doctor received them. The Government stipulated that *doctors deliberately insert other things* into the bottles to make a different combination of a product [R. 168].

As Dr. Icke testified, it is impossible to say, without exact knowledge, just when the precipitation did occur.

The Government's unfounded and worthless opinion evidence, based on the improper hypothetical question, is most fully disproved by the testimony of the appellant Bavouset and the witness Smiley. Bavouset testified that there was no precipitate in the bottles at the time he made the product, that there was no precipitate in the bottles when they were shipped to Dr. Ryerson on June 18, 1946 [R. 118], and that control batches were kept

until after the material had been shipped [R. 119]. Mrs. Smiley, in charge of the shipping department, positively testified that there were no foreign particles in these vials when she examined them for that purpose when they were shipped [R. 121].

Specification of Errors.

Appellants will rely on all of the points or assigned errors contained in the STATEMENT OF POINTS WHICH APPELLANTS INTEND TO RELY ON THE APPEAL, PURSUANT TO RULE 19(6) OF THIS COURT, namely, I to XII inclusive. These points or assigned errors appear at pages 229 to 232 inclusive of the Record.

In the argument the assigned errors will be considered in certain groups to facilitate presentation of the argument.

Summary of Argument.

Appellants are guilty of a crime only if the drugs were adulterated or misbranded at the time they were introduced by appellants into interstate commerce. The Government failed to prove how the goods were handled, the conditions of temperature, light, etc., to which they were exposed, and what was done with them or to them.

There is considerable evidence showing that these drugs will change in potency (Counts I, II, III and IV) or precipitate (Count VII) if subjected to undue light, improper temperatures, etc., or if other materials are added to the contents of the vials, etc.

The Government failed to eliminate the possibility of the drugs having lost their strength (Counts I, II, III and IV) or having undissolved material formed or introduced in it (Count VII) between the dates of shipment and the dates of the Government tests [Specification of Errors X and XI, R. 232]. POINT ONE, *infra*.

The positive testimony of appellants proves that the drugs were properly labeled and of the proper potency and purity when shipped.

The Trial Court permitted the Government attorney to propound improper hypothetical questions to the Government expert witnesses, some of which questions did not include a sufficient factual basis necessary to support an opinion, and other hypothetical questions which assumed facts which were never proved—assumed facts with respect to which there is no testimony whatever in the Record. Appellants' attorney's objections to these improper questions were overruled and the Government's expert witnesses were permitted to give their opinions to the prejudice of appellants [Specification of Errors I, II and III, R. 229 to 231, inclusive].

It is, of course, well established law that in criminal cases the identity of the object must be established, and in Food and Drug cases it is necessary to have a factual basis upon which the Government expert can testify as to the condition of the goods when they were placed in interstate commerce. The Government must prove that no changes in the drugs occurred subsequent to their be-

ing placed in interstate commerce, and as a foundation for such proof it is absolutely necessary that the Government establish the facts which show the conditions to which the goods were exposed, that they were not tampered with, etc. In the absence of such evidence appellants' objections to the hypothetical questions should have been sustained. POINT TWO, *infra*.

Without these answers to the hypothetical questions there would not be in the Record even an opinion that the goods were adulterated or misbranded when they were introduced into interstate commerce. Thus it is clear there is no proper admissible evidence upon which a finding of guilty could be made against either of the appellants [Specification of Error IV, R. 231], and that the finding of guilty is contrary to law [Specification of Error V, R. 231].

The failure of the Government to prove how the drugs were handled, the conditions to which they were exposed, or what was done with them or to them, and the failure of the Government to eliminate the possibility of the drugs having lost their strength or having become impure between the dates of shipment and the dates of the Government tests, clearly shows that the Government certainly failed to prove its case beyond a reasonable doubt [Specification of Errors VIII and IX, R. 231, 232]. POINT THREE, *infra*.

The positive evidence of appellants proves that the drugs were properly labeled and of proper potency and

purity when shipped. The finding of guilty by the Trial Court is, therefore, contrary to the weight of the evidence [Specification of Error VI, R. 231]. This positive testimony should compel a holding that appellants are not guilty of committing any crime. POINT THREE, *infra*.

The Government has not proved adulteration or misbranding because of the absence of "thyroid substance" as charged in Counts I and II. The positive testimony of appellants proves that there was one grain of aqueously extracted thyroid substance per cubic centimeter of the product Indoform. POINT THREE, *infra*.

The test made by the Government witness Mason for posterior pituitary was inaccurate and worthless. Mason did not take into consideration the fact that Ex. 3 contained suprarenal cortex which contains adrenalin, and that adrenalin represses any tests which are made to show the presence of posterior pituitary. POINT THREE, *infra*, section entitled "The Test Made By Mason for Posterior Pituitary Was Inaccurate and Worthless."

ARGUMENT.

POINT ONE.

Specification of Errors X and XI. [R. 232.]

“X.

“The District Court erred in that the Government failed to eliminate the possibility of the products having lost their strength or potency through the failure or neglect of parties other than the defendants” [R. 232].

“XI.

“The District Court erred in that the Government failed to prove that heat, or light, or lack of refrigeration, or moisture did not in some way come in contact with the bottles so as to cause the alleged loss of strength” [R. 232].

Appellants are not guilty of the crime charged unless the drugs were “* * * when caused to be introduced and delivered for introduction into interstate commerce * * *”¹ “* * * was then and there adulterated within the meaning of 21 U. S. C. 351(c) * * *”² or “* * * was then and there misbranded within the meaning of 21 U. S. C. 352(a) * * *.”³

The sole evidence of the Government to “prove beyond a reasonable doubt” that the drugs were adulterated or misbranded when placed in interstate commerce by appellants, are the opinions of its expert witnesses, which opinions are based on tests made after the drugs were picked up at the doctors’ offices to whom the drugs were

¹These words are quoted from the counts of the information. See, for example, Count I [R. 3] starting at line 11 at the bottom of the page.

²Counts I, III, V and VII charge adulteration.

³Counts II, IV and VI charge misbranding.

shipped, and after the drugs had been shipped to Washington, D. C.

The Government's charge of adulteration and misbranding because of the absence of iodine from the Indoform, Exs. 1 and 2, as charged in Counts I and II, will be separately discussed under the section in POINT THREE entitled "Government Has Not Proved Adulteration or Misbranding Because of the Absence of 'Thyroid Substance' as Charged in Counts I and II."

We respectfully submit that the opinion evidence of the Government is absolutely worthless because the expert witnesses had no knowledge that the alleged adulteration or misbranding did not occur enroute to the doctor's office, or in the doctor's office, or in the hands of the Government inspectors who picked up the drugs, or enroute to Washington, D. C., when shipped there by the Government inspectors.

As this is a criminal case it was, of course, incumbent upon the Government to prove the charges in the information by evidence that satisfies beyond a reasonable doubt that the appellants were guilty of the charges.

Alberty v. United States (C. C. A. 9), 159 F. (2d) 278;

Von Bremen v. United States (C. C. A. 2), 192 Fed. 904;

George A. Breon & Co., Inc. v. United States (C. C. A. 8), 74 F. (2d) 4;

United States v. Commercial Creamery Co. (D. C. Wash.), 43 Fed. Supp. 714.

To establish its case the Government had to prove that the drugs did not change in potency or become impure after they were shipped by appellants.

In this type of case such evidence is usually given by the receiver of the drugs and by the Government inspector who collects the drugs, both of whom must testify as to how the drugs were handled and cared for while in their custody; otherwise there is no factual basis to support hypothetical questions such as were propounded to the witnesses, or to support the opinions given in response thereto.

These persons, or any persons who could testify as to how the goods were handled after being shipped by appellants, were not called by the Government, and evidence such as they might give is totally absent from this case.

Appellants sell their drugs only to doctors [R. 111]. The Government inspectors did not pick up the drugs from a drugstore where they are kept on shelves for open sale to customers and not for the druggist's own use. They were picked up at doctors' offices where doctors use these drugs in the treatment of their patients.

Not only is there a lack of evidence as to how the drugs were cared for after they were shipped by appellants, but, on the contrary, there are two important classes of evidence which establish beyond all doubt that the Government did not prove its case, and that the weight of the evidence is contrary to the Court's finding of guilty.

Stability of Appellants'
Products Under Heat, etc.

In the first place, there is considerable evidence showing that these drugs will change in potency if not kept under proper conditions of temperature, light, etc., and if not properly handled.

Dr. Icke testified, with respect to the stability of thiamine hydrochloride (Counts III and IV), as follows:

“Q. What would you assume to be above normal conditions on B-1 as far as temperatures are concerned?

* * * * *

A. I would say that any temperature above 100 to 120 degrees Fahrenheit might be above what you would consider normal.

Q. If the bottle was sealed as in that bottle, would you expect it to deteriorate within a matter of a few months down to only 33½ per cent? A. If that bottle had been setting in the sunlight so that the temperature got up high, or any other factor which might have elevated the temperature, it might have deteriorated.” [R. 185.]

* * * * *

“Q. Under what conditions is it not a stable product? A. Vitamin B-1 can be destroyed very rapidly if the solution is brought towards neutrality or on the alkaline side in a solution that must be kept acid in order to be stable. Also, it is susceptible to destruction by presence of sulfites, or it can be destroyed by oxidation, and in any of those cases that those agents were present which might cause destruction, any temperature above normal would speed the rate of destruction.” [R. 159.]

He also testified that many doctors use isopropyl alcohol for sterilizing instruments and that even a small amount of isopropyl alcohol would affect the stability of the thiamine hydrochloride [R. 161, 163]. Dr. Icke also testified that air which contains oxygen would affect the stability of thiamine hydrochloride in that thiamine is susceptible to oxidation [R. 163].

Bavouset testified that thiamine hydrochloride [Counts III and IV, Exs. 6 and 7] will deteriorate if subjected to light or heat, or if exposed to air over a period of time, or if the degree of acidity of the solution is changed from pH 3.2, and that if the solution becomes neutral, the thiamine hydrochloride dissipates very rapidly [R. 115, 149, 150].

With respect to the undissolved material in Ex. 1 (Count VII), Dr. Icke testified that riboflavin might precipitate if the doctor added other material, changing the nature of the solvent, and that temperature would affect its stability, particularly if any oxidizing materials or any substance which increased the alkalinity of the solvent were introduced into the solution [R. 171, 172].

Wiley stated that temperatures slightly above freezing would hasten or increase precipitation [R. 42].

Bavouset testified that he has noticed that riboflavin precipitates upon fluctuation of temperature [R. 145].

Addition of Other Things Into Products.

In the second place, the evidence shows that doctors insert hypodermic needles into the caps of these bottles for withdrawing the solution from them, and that it is possible and likely that the potencies of the solutions will be changed because of the presence of isopropyl alcohol

which some doctors use for sterilizing hypodermic needles, or the hypodermic needles themselves [R. 162].

Dr. Icke's testimony on this point is on pages 161, 162 and 163 of the Record and reads as follows:

“Q. Are you familiar with the methods used by doctors in their offices? A. Yes, sir.

Q. In handling bottles, hypodermic syringes, etc.? A. Yes.

Q. Do doctors sterilize their syringes and needles before they take out doses of medicine from bottles of that kind? A. It is the common practice to sterilize them, yes.

Q. And what things are used for that purpose? A. Well, sometimes they use steam sterilization, or heating the things in boiling water. Others may use bichloride of mercury or various other bacteriacides. Also, it has become more and more common in recent years to use isopropyl solutions for sterilizing instruments.

Q. Before a bottle of that character is used for the purpose of withdrawing a dose of medicine is it customary to sterilize with some substance the cork before the needle is inserted? A. Yes. The doctor usually takes a piece of cotton or gauze and wipes off the top of the cap with alcohol, isopropyl alcohol is often used.

Q. If any of that isopropyl alcohol was left in the needle and went into the bottle would it affect the content or the potency of the thiamine hydrochloride? A. It might, because isopropyl alcohol is known to contain bacteriacides under many conditions. I have worked in a chemical laboratory at the time that discovery was made and observed the experimental work of the investigator, who showed that

isopropyl alcohol often contains bacteriacides. And I have also seen doctors taking solution to be injected from this bottle in which they have used isopropyl alcohol to sterilize their needle and syringe, and often, instead of drying the needle and syringe, they may just put the needle onto the syringe and move the plunger back and forth to pass a little air through it and get rid of most of the sterilizing agent. But I have seen them insert a needle into a bottle and which it was not completely dry, and because of their practice, introduce air into it. It would be possible for a spray of a small amount of isopropyl alcohol, and, therefore, bacteriacide, to be introduced into that bottle.

Q. And would the amount that would be so introduced affect the thiamine hydrochloride in the bottle?
A. It would depend entirely on how much bacteriacide was in the isopropyl alcohol, how many injections had been withdrawn from the bottle, and how much bacteriacide was there just how much it would affect it. But even a small amount would affect it.

The Court: Immediately?

The Witness: The effect would start immediately; yes."

In addition to this we have the stipulation, and we believe this is very important, of the Government that the doctors deliberately insert other things into bottles to make a different combination of a product.

"Q. Do they ever deliberately insert other things into bottles to make a different combination of a product?

Mr. Neukom: Your Honor, I will stipulate that they do." [R. 168.]

The Government witness Capps admitted that he made no examination of the cap on Ex. 7 to determine whether or not it was punctured in any way, other than by just looking at it [R. 106]. Dr. Icke's testimony is that you can't tell whether or not a cap has been punctured by looking at it just with the naked eye [R. 161].

Government witness Mason was asked by the Court if the cork was sealed in the bottle, Ex. 5, in any way, and he stated, "I do not remember whether it was sealed into the bottle or not. * * *" [R. 78]. Also, the Government witness Mason, after testifying it was common practice for doctors to pass a hypodermic needle through the rubber cork [R. 79], testified that he did not examine the cork to determine whether or not it had been punctured by a needle (hypodermic needle), he stated he did not make an independent investigation on that point [R. 80].

The Government witness Mason took the stand on rebuttal and contradicted his original testimony by stating with regard to Ex. 3, "The vial was full and the rubber stopper or cork was protected, with a celluloid seal around it when I received it. It appeared as if it had never been opened." [R. 215.] After his testimony to the contrary this later testimony certainly does not establish the facts and does nothing more, it is submitted, than detract from the weight of any of Mason's testimony.

In this connection please see *United States v. Lord-Mott Co.*, 57 Fed. Supp. 128, in which the Court states at page 132:

"* * * But the Court can not blink the fact that they (the witnesses for the Government) are naturally interested, or biased, in seeing that their work or the work of their associates in this matter is upheld, * * *." (Parenthesis added.)

Thus your Honors will see that if the drugs were not properly handled, or if the hypodermic needles used contained certain chemicals, or if the doctors from whose offices the drugs were picked up had injected other things into the bottles to make a different combination, it is quite likely that the potencies and conditions of the products changed at that time.

In addition to this there is no evidence that the Government inspector properly handled the drugs after he picked them up. Anyone of the above things may have occurred even while in the inspector's hands, or during shipment by the inspector to Washington, D. C.

The probabilities and possibilities mentioned above become even more important in view of the testimony of the appellant Bavouset and appellants' witnesses Smiley, whose testimony establishes that when the materials were compounded they were of the potencies specified on the labels, and when shipped were inspected for the presence of impurities. Point Three, *infra*.

It seems quite reasonable to conclude, in view of these facts, that the drugs were not adulterated or misbranded when shipped, and the Court must reach the conclusion that the Government has not established its case nor carried the burden required in criminal cases.

The Court cannot assume that the various things which might happen to the drugs did not occur. This is a criminal case. There is imposed on the Government the burden of proving its case beyond a reasonable doubt, and the legal decisions hold that the Government has not proved its case beyond a reasonable doubt, unless it proves that the object or thing introduced in evidence was in the same condition at the time when the Government tests

were made, as it was at the time of the occurrence of the crime charged, namely, in this case, at the time the goods were introduced into interstate commerce.

**Law re Goods Being of
Same Potency and Condition When
Tested as When Shipped.**

In *United States v. S. B. Penick & Co., et al.*, 136 F. (2d) 413, the Circuit Court of Appeals for the Second Circuit upheld the conviction by the Lower Court and rejected the argument of appellants that the Government had not proved that the samples tested by the Government were the same drugs as introduced into interstate commerce. In that case the Court said:

“* * * It is true that before a physical object connected with the commission of a crime can properly be admitted in evidence, there must be a showing that such object is in substantially the same condition as when the crime was committed. 2 Wharton, Criminal Evid., 11th Ed., § 757. * * * In each case the trial judge before he admits it in evidence must be satisfied that in reasonable probability the article has not been changed in important respects. Wigmore, Evidence, 3d Ed., § 437 (1); 32 C. J. S., Evidence, § 607. *In reaching his conclusion he must be guided by the nature of the article, the circumstances surrounding the preservation and custody of it, and the likelihood of intermeddlers tampering with it.* * * *” (Italics added) (p. 415.)

The Circuit Court, after these quotations, pointed out that in that case when the goods were received by the party to whom they were shipped by appellants, *samples* were taken and *preserved* and that it was a part of these samples which were obtained and tested by the Government witnesses. Thus in the *Penick* case the Government

introduced evidence which showed that the drugs were properly cared for and thus, by such evidence, excluded the possibility that the drugs became adulterated or misbranded after appellants had introduced them into interstate commerce.

Another case is *United States v. Buffalo Pharmacal Co., Inc.*, 131 F. (2d) 500, wherein the Circuit Court of Appeals for the Second Circuit upheld the conviction of one of the appellants because there was some evidence to indicate that the bottle of digitalis in question had been properly cared for. In that case evidence was introduced by appellants to show that digitalis, if not properly cared for, might deteriorate. The Government, to meet this evidence, showed that the goods were properly cared for. The Court said:

“* * * While cross examination brought out that digitalis tablets may deteriorate in potency by lapse of time if not properly stored, *there was some testimony to indicate that the bottle in question had been properly cared for.* We cannot say that the evidence was insufficient to support the verdict of adulteration and misbranding.” (Italics added) (p. 502.)

In this case there is absolutely no evidence whatsoever that the drugs shipped by appellants were properly cared for or used by the doctors who received them or by the Government inspectors who picked them up.

In *Novak v. District of Columbia*, 49 A. (2d) 88, the Court stated at page 90:

“* * * We agree that it was still incumbent upon the government to prove that the specimen taken from defendant and the one analyzed by the

chemists, and reported on in court, were the same and were in substantially the same condition when tested as when taken. * * *

32 Corpus Juris Secundum, Section 607 at page 458, reads in part as follows:

“In order that an article may be introduced it must be satisfactorily identified, and it must also be shown to the satisfaction of the Court that no such substantial change in the article exhibited as to render the evidence misleading has taken place. * * *

“*Samples.* Samples are admissible on an issue as to the properties or qualities of the substance or articles involved in the case. The samples must be sufficiently identified as to their source, and must reflect the condition of the substance or articles as of the time involved in the issues. * * *

In *Gutman v. Industrial Com.*, 50 N. E. (2d) 187, the Court held at page 188:

“‘It must appear, as a preliminary to the introduction of any object in evidence, that it has not sustained any substantial change by reason of lapse of time or otherwise, since the time in issue.’ 20 Am. Juris 602, Section 719.”

In *Rosa Alma Kees v. Canada Dry Ginger Ale, Inc.*, 199 S. W. (2d) 76, the defendant sold carbonated water to a grocer. The bottles were placed on a shelf in the grocery store, and the store was so arranged that the customers could wait on themselves. The owner of the store, Lovell, said that he was there most of the time, that nothing in the store ever froze, and that the bottles had not been tampered with.

The plaintiff who bought two bottles took them home, and in handling they exploded and she was very seriously injured. She brought suit against the defendant bottling company and tried her case under the *res ipsa loquitur* doctrine. In connection with this doctrine the Court stated as follows:

“* * * This doctrine is a rule of evidence that relates to the mode of proof and is applicable where there has been an unexplained accident, and the instrument causing the injury was under the management or control of the defendant and, in the ordinary course of events, the accident would not have happened if the defendant had used due care. The unexplained circumstances may, in a particular case, warrant an inference of negligence. The doctrine has been extended to apply to cases involving an exploding bottle of beverage where it is shown that the condition of the bottle was not changed after it left the bottler’s possession and prior to the occurrence causing the injury. When all intervening causes have been eliminated then, in effect, the bottle is still regarded as though it continued to remain in the hands of the bottler. (See *Stolle v. Anheuser-Busch, Inc.*, 271 S. W. 497; *Tayer v. York Ice Machinery Corp.*, 119 S. W. (2d) 240, 244.) In *Hughes v. Miami Coca Cola Bottling Co.*, 19 So. (2d) (Fla.) 862, 864, the court said: ‘So far as we have been able to find from a study of the decisions, no court has ever held that recovery may be had in such cases, under the *res ipsa loquitur* doctrine, without an affirmative showing on the part of the plaintiff that after the bottle left the possession of the bottler it was not subjected to any unusual atmospheric changes or changes in temperature, or that it was not handled improperly up to the time of the explosion.’” (pp. 76, 77.)

After discussing the retailer's testimony and holding that there is no question but that "Lovell should not have been permitted to testify that the bottles were not tampered with while in his store and that the bottles and caps were not changed while in his store." on the ground that "in these matters the witness was indulging in mere speculation, guess and conclusions," the Court, in reversing the lower Court, held:

"* * * The bottle may have been frozen or subjected to extremely cold temperature before it reached Lovell's store. It may have been dropped, cracked, tampered with or mishandled by the customers or the employees while it was on the shelf in Lovell's store. It was there approximately 30 days. Certainly the jury was required to indulge in guess and speculation in finding that between the time that the bottle left the possession of the defendant and when it came into possession of the plaintiff it was not subjected to any condition that would tend to bring about the explosion resulting in plaintiff's injury.
* * * citing cases * * *." (p. 79.)

See also *Pilot Life Ins. Co. v. Wise* (C. C. A. 5), 61 F. (2d) 481, at page 483.

POINT TWO.

Specification of Errors I, II and III [R. 229, 230, 231].

“I.

“The District Court erred in overruling defendants’ objection to the latter of the following questions propounded to the witness Wiley:

‘Q. By Mr. Neukom: Dr. Wiley, taking the two vials, part of Government’s Exhibit No. 1, which I understand you examined about six weeks after the shipment in question here, from your knowledge of sterile solutions and from your observation of sterile solutions, your experience, are you able to express an opinion to this court as to whether or not the contents of those two vials, Government’s Exhibit 1, did contain the undissolved particles you noticed there then as of the date they were shipped, namely, on or about June 18, 1946? Your answer is yes or no.’

* * * * *

‘Q. By Mr. Neukom: Will you please relate your opinion?’ [Rep. Tr. of Proceedings, p. 17, lines 9 to 18, and p. 18, lines 17 and 18.]” [R. 229, 230.]

“II.

The District Court erred in overruling defendants’ objections to the following questions put to the witness Mason:

‘Q. Assuming, Mr. Mason, that this product was not exposed to excessive temperatures, that is to say, that you said was 212 degrees is the destructive temperature; and assuming the product was handled in a normal and careful manner, retained in the bottle, as Government’s Exhibit No. 4, I believe; assuming which bottle you opened and conducted the tests as you have testified; and, with the assumption of what you found or did not find at that time, have you an opinion as to whether or not this product contained

three international units of posterior pituitary on September 17, 1945?’

* * * * *

‘Q. By Mr. Neukom: Now assuming that all that you have testified to here and the explanations you have given, what is your opinion, carrying on the assumptions that I have enumerated—what is your opinion as to the amount, if any, of posterior pituitary was in the product on or about September 17, 1945?’ [Rep. Tr. of Proceedings, p. 61, lines 16 to 25, and p. 62, lines 6 to 10.]” [R. 230.]

“III.

The District Court erred in overruling defendants’ objections to the following questions put to the witness Capps:

‘Q. Now, assuming that the product received ordinary and reasonable care, and was not exposed to excessive heats, such as heats any more than would be normal from shipping and the weather, and basing upon what you found on September 24, 1945, the amount of the B-1 or thiamine chloride that you found, have you an opinion as to what percentage or what amount that product, substance, or solution had on or about July 16, 1945, the date it was originally shipped?’ [Rep. Tr. of Proceedings p. 94, lines 12 to 19.]” [R. 231.]

It was prejudicial error for the Trial Court to allow the Government’s witnesses to answer these hypothetical questions. The appellants were seriously prejudiced thereby, particularly since there is no other competent evidence to sustain a conviction.

Subtract from the evidence these improper hypothetical questions and the unfounded opinion answers given in response to them, and what evidence of guilt is there? Absolutely none.

The first of said improper questions (Specification of Error I) was in connection with Ex. 1 (Count VII) and was directed to the witness Wiley. These questions appear on pages 41 and 42 of the Record. The objection appears on page 41 of the Record and is as follows:

“Mr. Stick: I object to that, your Honor, upon the ground that until the conditions under which these bottles have existed or to which these bottles and contents have been subjected since the date that they were put into interstate commerce on June 18th must be before this witness before he can express an opinion as to whether or not the contents that are in there now were in the condition that it is now, going back to June 18th when it was shipped.” [R. 41, 42.]

These hypothetical questions were bad and improper in that they did not contain sufficient facts to afford ground for a reasonable conclusion or opinion.

The record is clear that the riboflavin in Ex. 1 will precipitate if subjected to coolness, temperature fluctuations, if foreign material is added, etc. (POINT ONE, *supra*) and yet no mention whatever is made in said hypothetical questions with respect to the conditions to which Ex. 1 was subjected.

**Law re Hypothetical Question
Presenting Sufficient Facts
to Afford Ground for
Reasonable Conclusion.**

“* * * Purely abstract or theoretical questions and those too vague or indefinite to permit the witness to form a judgment of any value should be excluded.
* * * A question is ordinarily improper where it does not present sufficient facts to afford ground for a reasonable conclusion.”

32 Corpus Juris Secundum, Section 551.

In *Bickford, et al. v. Lawson*, 27 Cal. App. (2d) 416, 81 P. (2d) 216 at pages 222 and 223, the Court applied this rule of law as follows:

“Where the facts related in the hypothetical question omit material undisputed evidence necessary to a fair, intelligent and sound opinion of the witness regarding the problem to be determined, it is not error for the court to sustain an objection thereto. The chief test of the competency of a hypothetical question which seeks to elicit the professional opinion of a physician regarding the treatment of a patient is whether it is a full and fair recital of all the essential evidence disclosed by the record on the particular issue which is involved. Where the question assumes facts in direct conflict with the undisputed evidence, or omits material facts upon which a determination of the problem depends, the hypothetical question becomes misleading and it is then likely to lead the witness to a false conclusion, and should be rejected.

* * *

See also:

Harrison v. United States (D. C. Pa.), 49 F. (2d) 948 at page 949.

See also *Lawrence v. Butler*, 240 Pac. 840, 79 Cal. App. 436. In this case a truck damaged plaintiff's automobile after slipping down hill from oil in the street. Objections to hypothetical questions as to whether the truck would slide back if effective brakes were applied were *held* to have been properly sustained, since the element of the greasy condition of the pavement was not included.

The second of said improper questions (Specification of Error II) was in connection with Ex. 3 (Counts I and II) and was directed to the witness Mason. These questions appear on pages 75 and 76 of the Record. The objection

appears on pages 74 and 76 of the Record and is as follows:

“Mr. Stick: I object to that as a matter that cannot be testified to by this gentleman, unless all of the conditions and factors under which this matter was kept, handled and existed between the time when it was shipped by the defendant to the time when he first saw it is also before him.” [R. 74.]

This hypothetical question was bad and improper in that it included facts which were assumed, which assumed facts are not supported by any evidence whatever in the case. There is no evidence whatever in the case that the “* * * product was not exposed to excessive temperatures * * *” or that it “* * * was handled in a normal and careful manner * * *” [R. 75].

The third of said improper questions (Specification of Error III) was in connection with Ex. 5 (Counts III and IV) and was directed to the witness Capps. This question appears on pages 100 and 101 of the Record.

This hypothetical question, like the second one, was bad and improper in that it included facts which were merely assumed and which were not supported by any evidence whatever. The record is entirely devoid of any evidence whatever to the effect that the “* * * product received ordinary and reasonable care and was not exposed to excessive heats, such as heats any more than would be normal from shipping and the weather, * * *” [R. 100].

In fact, there is no evidence whatever as to the conditions to which any of the products were exposed, or what was done to or with any of them from the time the products were introduced into interstate commerce at Pasadena, California, until tested by the Government witnesses at Washington, D. C.

Furthermore, the evidence clearly shows that these products, Ex. 3 (Counts I and II) and Ex. 5 (Counts III and IV) will deteriorate if subjected to heat, light or air, or if other substances are added thereto. (POINT ONE, *supra.*)

**Law re Hypothetical
Question Must Be Based
on Facts in Evidence.**

The applicable law was stated by this Court in the case of *Travelers Ins. Co. v. Drake*, 89 F. (2d) 47, at page 50, as follows:

“* * * When the question assumes a state of facts which the evidence directly, fairly, and reasonably tends to establish, and does not transcend the range of the evidence, it is not objectionable. *Denver & R. G. Ry. Co. v. Roller* (C. C. A.) 100 F. 738, 49 L. R. A. 77; *Proechel v. U. S.* (C. C. A.) 59 F. (2d) 648. * * *.”

In *Philadelphia & R. Ry. Co. v. Cannon* (C. C. A. 3), 296 Fed. 302, the Court held at page 306 as follows:

“* * * It scarcely needs the citation of authorities to sustain the proposition that a hypothetical question calling for expert opinion must be based on facts in evidence. We are of opinion, therefore, that the question was improperly framed and the answer erroneously admitted. * * * (citing cases) * * *.”

In *North American Accident Association v. Woodson* (C. C. A. 7), 64 Fed. 689, the Court stated on pages 691, 692 and 695, as follows:

“Seven assignments of error, numbered from the fifth to the eleventh, inclusive, relate to the admission of evidence of expert witnesses concerning the cause of Dr. Kemper’s death, in answer to hypothetical questions framed upon a supposed state of

facts not appearing in evidence at the time the questions were put, and not proven at any time on the trial. This testimony, against defendant's objection was introduced by means of depositions which had been taken before the trial, mainly in the state of Missouri. Several physicians residing in Missouri were examined, and their testimony taken, presumably on the supposition that the supposed facts upon which the answers were predicated would be proven by means of other witnesses on the trial. Some of these facts were proven, while others were not, but the answers were admitted by the court, the same as though all the facts stated in the hypothetical questions had been proven. This we think was error for which the judgment must be reversed. * * *” (pp. 691, 692).

“* * * It is a proposition too simple to require any citation of authorities that the material facts assumed in a hypothetical question must be proven on the trial, or rather that there must be evidence on the trial tending to prove them. Otherwise, it is error to allow them to be answered. * * *” (p. 695).

Jones, “The Law of Evidence in Civil Cases” (4th Ed), Section 371, page 694, states the applicable rule of law as follows:

“If there is no testimony in the case tending to prove the facts which are assumed by the hypothetical question, such question is improper.”

See also:

32 Corpus Juris Secundum, Sections 551 and 552:
Henkel v. Varner (U. S. Court of Appeals, D. C.).
138 F. (2d) 934.

**Hypothetical Questions Were
Also Improper in That an Expert
Witness Cannot Give His Opinion
Upon the Very Question in Issue.**

The testimony of expert witnesses is, of course, subject to the general rule excluding the opinions of experts as to the ultimate issues of fact to be determined. All of the hypothetical questions violated that rule of law and were therefore bad and improper. Appellants' attorney's objections to said questions should have been sustained on that ground, if for no other reason.

United States v. Spaulding, 293 U. S. 498, in which the Court held at 506, 507, as follows:

“* * * The medical opinions that respondent became totally and permanently disabled before his policy lapsed are without weight. * * * Moreover, that question is not to be resolved by opinion evidence. It was the ultimate issue to be decided by the jury upon all the evidence in obedience to the judge's instructions as to the meaning of the crucial phrase, and other questions of law. The experts ought not to have been asked or allowed to state their conclusions on the whole case. (Citing cases.)”

See also:

United States v. Stephens (C. C. A. 9), 73 F. (2d) 695, 701;

United States v. McCreary (C. C. A. 9), 105 F. (2d) 297, 299;

Farris v. Interstate Circuit (C. C. A. 5), 116 F. (2d) 409.

POINT THREE.

Specification of Errors IV, V, VI, VII, VIII and IX

Inclusive [R. 231, 232].

“IV.

The District Court erred in that there is no evidence in this case upon which a finding of guilty could be made against either of the defendants.” [R. 231.]

“V.

The District Court erred in that the finding of guilty is contrary to law.” [R. 231.]

“VI.

The District Court erred in that the finding of guilty is contrary to the weight of the evidence.” [R. 231.]

“VII.

The District Court erred in that the finding of guilty is not supported by substantial evidence.” [R. 231.]

“VIII.

The District Court erred in that it did not give defendants the benefit of reasonable doubt which they were legally entitled to.” [R. 231.]

“IX.

The District Court erred in that the evidence in this case did not demonstrate beyond a reasonable doubt the defendants’ guilt.” [R. 232.]

**There Is No Admissible Evidence in
the Case to Sustain the Finding
of Guilty.**

Even without any evidence on behalf of appellants, the Government failed to prove its case. At the close of Government’s case the sole evidence of guilt was the unfounded opinion answers to Government’s hypothetical questions which assumed facts not supported by any evi-

dence whatever, or which did not include sufficient facts to support an opinion answer.

As we have shown in POINT Two, *supra*, appellants' attorney's objections to these questions should have been sustained, and it was prejudicial error for the Trial Court to allow the Government's witnesses to answer these improper questions.

Furthermore, even if the questions directed to the witness Wiley (Count VII) were proper, his answers thereto are not entitled to any weight whatever. These questions were bad and improper for the reason that they did not include a sufficient factual basis to support an opinion in that no mention whatever was made with regard to the conditions to which the product had been subjected. (POINT Two, *supra*.)

In connection with this Count, it should be noted that there is no evidence in the case as to what the undissolved material in Ex. 1 is. Dr. Thienes testified he could not tell what the precipitate was without chemically testing the precipitate [R. 54]. As a matter of fact, there is no evidence that the particles in Ex. 1 are precipitates; there is no evidence that these particles do not constitute material which was added to the vials after the doctor received them.

Wiley testified that Ex. 1 (Count VII) was twenty times over-saturated [R. 46]. He based this statement upon the solubility of riboflavin in water. He failed to take into consideration the fact that Indoform (Ex. 1) contains nicotinamide which is a very fine solvent for riboflavin and very definitely increases the solubility and stability of the riboflavin [R. 145]. In other words, the solvent is not the pure water, but a solution containing

other materials besides riboflavin and water [R. 167]. Some products have as much as 5.3 milligrams of riboflavin per cubic centimeter of solution [R. 167]. Ex. B, a competitor's product, contains 4 milligrams of riboflavin per cubic centimeter [R. 167].

In the light of the other substances in Ex. 1, as Dr. Icke stated, the two milligrams of riboflavin were not an excessive amount and it was not a supersaturated solution of riboflavin [R. 170].

As Dr. Icke testified, “* * * It would be impossible to say, without exact knowledge, just when that precipitation did occur. * * *” [R. 170]. As shown in POINT ONE, *supra*, the undissolved material in the product might be due to any one of a number of factors, and undoubtedly first appeared after the product was shipped.

As we have shown in POINT ONE, *supra*, there is no evidence as to how the products were handled or of the conditions to which they were subjected. Furthermore, there was no evidence precluding the possibility that the drugs became adulterated and misbranded at some time after they had been shipped by appellants from Pasadena, California [Specification of Errors X and XI, R. 232].

There was no proper or admissible evidence in this case upon which a finding of guilty could be made against either of the appellants. As a matter of fact, there is no proper evidence supporting the Lower Court's findings of guilty [Specification of Errors IV, VI and VII, R. 231]. The Lower Court's findings of guilty were most certainly contrary to law, which requires proof beyond a reasonable doubt [Specification of Errors V, VIII and IX, R. 231, 232].

**Appellants Proved by Positive
Evidence That Products Were Not
Adulterated or Misbranded When
Introduced Into Interstate Commerce.**

At the conclusion of the Government's case, appellants were entitled to a dismissal; but in order to show by positive evidence that the drugs were not adulterated or misbranded at the time they were introduced into interstate commerce, appellants produced witnesses who testified of their own personal knowledge as to the compounding of the drugs and their condition at the time of shipment.

With respect to Exs. 3 and 4 (Counts I and II), the appellant Bavouset testified that he personally made a quantity of Indoform [R. 109] and when he made it it contained all of the ingredients specified on the label. He said:

"Q. And this was one of several that were shipped to him. At the time that that was shipped was there three international units of posterior pituitary in a cubic centimeter of the contents of that bottle?

A. Yes. I measured out that amount for this particular solution.

"Q. And was there one grain of thyroid substance in that matter at that time? A. There was aqueously extracted one grain per cc of thyroid" [R. 110].

Bavouset testified that he probably made Ex. 6 (Counts III and IV), stated in detail how all of the materials named on the label were combined in the solution, and at that time the solution had the full strength and potency that is set forth on the label [R. 114, 115].

With regard to Ex. 1 (Count VII) Bavouset testified:

"Q. I will ask you to look at the two bottles in Exhibit 1, look through them. Do you see anything

in those bottles other than the liquid solution? A. Yes; there is a precipitate.

Q. Was that precipitate in those bottles at the time you made it? A. No; it was not.

Q. Or when you finished making it? A. No; it was not.

Q. Was that precipitate in those bottles when you shipped it to Dr. Ryerson on June 18, 1946? A. No; it was not.

Q. Before any of these materials are shipped have you any means in your office of checking these products? A. We keep control batches for a short time after the material has gone out of the business, or the place of business.

Q. Are there any inspections made at the time they are shipped out? A. Yes; a very careful inspection is made the last thing before it is placed in shipping cartons and sent out and marketed" [R. 118, 119].

Mrs. Smiley testified that she is employed at Pasadena Research Laboratories, in charge of the shipping department, and was so employed on June 18, 1946 [R. 120]. Mrs. Smiley checks the solutions in the vials to be sure there are no foreign particles before the vials are put on the invoice on another table for the next girl to package and ship out [R. 120, 121]. Mrs. Smiley positively testified that there were no foreign particles in the vials, Ex. 1, (Count VII) when she examined them for that purpose, by means of an inspection lamp, at the time they were shipped [R. 121]. Mrs. Smiley believes she recalls this particular shipment because it is unusual to have an order as large as fifty bottles [R. 122].

Thus, we have only the Government's unfounded, improper, valueless opinion evidence, which is thoroughly

disproved by fact evidence of appellants. Thus we can see only one conclusion, namely, that the findings of guilty by the Lower Court are contrary to the weight of the evidence; or that there is no evidence to support the Lower Court's findings of guilty and that the Government utterly failed to establish its case beyond a reasonable doubt.

**Government Has Not Proved
Adulteration or Misbranding
Because of the Absence of
"Thyroid Substance" as
Charged in Counts I and II.**

We are arguing this charge separately because the Government takes the position that the label, Ex. 4, on the Indoform vial represents that iodine is present, and the Government witness Buell made a test for iodine and found none. It is appellants' position that the label does not indicate that iodine is present, but, on the contrary, clearly indicates that iodine is not present, and appellants furthermore admit that there never was any iodine in the sterile Indoform solution.

It is appellants' position, and we believe it is well supported by the facts, that in the absence of proof beyond a reasonable doubt there was not *any* thyroid substance present, the appellants must be found not guilty.

The label, Ex. 4, states that each cubic centimeter contains "Thyroid Substance 1 gr." and bears the notation, "This preparation does not contain any known therapeutically useful constituent" [R. 63].

The Food and Drug Act distinguishes between an "official drug" which is one defined in the Official Compendium, namely, the United States Pharmacopoeia, and an "unofficial drug" which is not defined. 21 U. S. C., Section 351(b) refers to the so-called official drug and a

person is guilty of an offense if the drug differs from the standards set forth in the Pharmacopoeia. In this present case, however, appellants are not charged with the violation of 21 U. S. C., Section 351(b). "Thyroid substance" is not an official drug. It is an unofficial drug. Appellants are charged with a violation of 21 U. S. C., Section 351(c), which states that a drug shall be deemed to be adulterated if "its strength differs from, or its purity or quality falls below that which it purports or is represented to possess" (21 U. S. C., Sec. 351(c)).

The crime charged is that this drug, sterile Indoform solution, was adulterated because at the time of shipment it was represented to contain "thyroid substance 1 gr. (per cc), * * * whereas, in fact and in truth, each cubic centimeter of said drug * * * did not contain 1 grain of Thyroid Substance but did contain no Thyroid Substance" [Count II, R. 4, 5].

The sole question then is "did this drug contain one grain per cubic centimeter of thyroid substance as set forth on the label when it was shipped," which thyroid substance "* * * does not contain any known therapeutically useful constituent" [Label, Ex. 4, R. 63]. The Government did not prove beyond a reasonable doubt that one grain of thyroid substance per cubic centimeter was not present. The only thing the Government attempted to prove was that there was no iodine present.

The Government's expert witness Buell did not test to determine the presence of any thyroid substance, other than that one substance, namely, iodine:

"A. The only thing I examined it for was for the therapeutically active ingredients of thyroid, which were the organically combined iodine products" [R. 95].

The label on the vial does not represent that iodine is present. The label unequivocally states that the preparation does not contain any known therapeutically useful constituents. Thus the label itself indicates that iodine is not present for the very reason that iodine is a therapeutically useful ingredient. Thus it is futile for the Government's witness to test for iodine. The Government should have tested the solution for the other thyroid substances.

The Government witness Buell admitted that there are fats, proteins and other substances present in the thyroid gland in addition to iodine [R. 93] and that in the solution which he tested there could be other parts of the thyroid gland in solution.

"Q. * * * There could, however, be other parts of the thyroid gland solution? A. That is possible" [R. 94].

Thus we believe the Government's own witness has clearly admitted: first, he only tested for the presence of iodine; and, second, that other thyroid substances could be present.

Now we believe it is very clear from the testimony of the Government's own witness Buell that the solution contained within the vial, Ex. 3, was not different from anything which it was purported or represented to possess.

The witness Buell admits:

"Q. Did you read on there this portion: 'This preparation does not contain any known therapeutically useful constituent'? A. I read that, sir.

Q. Did that indicate to you that there was no active substance of thyroid in that solution? A. Well, you would draw that conclusion from reading that; but I did not let that influence me at all when I made my analysis" [R. 94, 95].

This, we believe, is a vital admission and one which establishes most convincingly that the Government failed to prove its case. The Government's own witness Buell has admitted that he read the notation on the label which stated that the preparation did not contain any "known therapeutically useful constituent" and from that he did draw the conclusion that there was no active substance of thyroid in the solution. In other words, the Government's own witness admitted that from the label he did draw the conclusion that no iodine was present in the solution contained in the vial, Ex. 3.

Not only did the Government fail to prove thyroid substance was not present, but appellants, through the testimony of Bavouset, established by direct testimony as to how the solution was made, and that one grain of thyroid substance for every cubic centimeter of solution was embodied in the solution when it was manufactured.

Bavouset's testimony as to the disclaimer, how the solution was made and what it contained is as follows:

"* * * We put a disclaimer on that product, stating that it did not contain therapeutically useful constituents, to definitely let the doctor know that the thyroid content was not the iodine content" [R. 111].

"The Court: What do you mean by 'thyroid substance'?"

The Witness: You take the powdered thyroid, that is the dessicated thyroid, and put it into a flask containing water, a measured amount of water, and that is extracted by shaking it over a period of time, usually two weeks. That is not continuously shaken, but several times a day, shaken up thoroughly and allowed to stand and then filtered off, and

that material which is soluble in the water is then put into vials, with due process of sterilization, etc." [R. 111].

He also testified that he has been making this product over a period of about fifteen years [R. 110], that doctors request it and it is sold only to doctors [R. 111]. Bavouset also testified that there are many other preparations which specify "thyroid substance" that do not contain any iodine and that such preparations are used daily:

"The Court: Before you leave this thyroid question, I would like to ask the witness: Is there any other article on the market that you know anything about that has a label which specifies 'thyroid substance' that does not contain any iodine?

The Witness: Yes, your Honor; there are many such preparations similar to this one and with thyroid, alone; that is, there is thyroid substance by itself without other materials in with it. There are many such preparations on the market, used daily.

The Court: That contain no iodine?

The Witness: Yes, your Honor.

The Court: Sold to physicians?

The Witness: Yes, your Honor.

Q. By Mr. Stick: Do you have any of those substances? A. Yes, we do" [R. 113].

It should be noted that this product is a sterile solution and sold only to doctors who request it, and that there are many "* * * doctors who claim that there are other activities that can be attributed to thyroid other than the activity of the thyroxin itself" [R. 136].

As Dr. Icke testified, an aqueous extract of thyroid substance merely refers to that material which would be

dissolved by water from the dessicated thyroid gland and that a doctor, looking at the label, would not expect to find thyroxin in the solution:

“Q. Is there anything on that label which would indicate to a doctor whether that is a water-solution or extraction? A. The very nature of the product itself, the fact that it is a glandular extract, would indicate to him that it is a water-solution.

Q. Would he, looking at that label, expect to find, normally, thyroxin in the solution? A. Certainly not” [R. 177].

There is no testimony whatever of any one being misled by the term “thyroid substance”. If a doctor intends to give thyroid active material, namely, thyroxin, he gives it orally, and not by injection. Many gland products are active only by injection, but thyroid is unique in being active by mouth; and a great point of that is made in biochemistry, which every doctor is required to take [R. 178].

Furthermore, in support of this factual testimony, we have the admission by the Government witness Buell that the thyroid is a gland in the body of a living animal; that this gland contains certain compounds; and that *one* of these compounds or substances is iodine or is an iodine compound [R. 92]. The Government witness Buell also admitted, on page 93 of the Record, that there would be in a thyroid gland things other than iodine or thyroxine. Then again, in the record on page 94, after admitting that iodine would not be present in a water solution, that other portions of the thyroid gland could be.

Thus epitomizing the testimony, the Government witness admits: first, that from the label he did draw the

conclusion that no active substance of the thyroid was present, namely, iodine; second, that the only test made was for the presence of iodine; third, that the thyroid gland contains other substances; and, fourth, that these other substances may have been present.

If this actual situation is coupled with the testimony of Bavouset that he put one grain of thyroid substance in each cubic centimeter of the solution, we respectfully submit that not only has the Government failed to prove its case beyond a reasonable doubt, but on the contrary, the *appellants have proved beyond a reasonable doubt* that the proper stated amount of thyroid substance was present.

**The Test Made by Mason for
Posterior Pituitary Was Inaccurate
and Worthless (Counts I and II).**

The test made of Ex. 3 (Counts I and II) by Mason for posterior pituitary was inaccurate and worthless. Mason did not take into consideration the fact that the solution, Ex. 3, contained suprarenal cortex which invariably contains adrenalin, and that adrenalin "would repress any tests which were designed to show the presence of posterior pituitary" [R. 179].

The *effect of adrenalin is antagonistic to the effect of posterior pituitary*, and the posterior pituitary in Ex. 3 was not allowed to show its presence in the test made by Mason [R. 180]. In other words, adrenalin negatives the effect of posterior pituitary because *posterior pituitary will contract smooth muscle* and *adrenalin will relax smooth muscle* so that there is an *antagonistic effect* [R. 195].

Although the witness Mason contended that if adrenalin was present in Ex. 1, it would not have interfered with

any assay for posterior pituitary [R. 222], he admitted on page 224 of the Record that the *test* that he made was *not an assay*, and that the only way that the quantity of posterior pituitary present could be determined is by an assay for the presence of posterior pituitary. He further admitted that he had not made any test to determine the relative quantity of epinephrin (adrenalin) present in a given amount of suprarenal cortex [R. 225], and that *if adrenalin were present before you could measure the presence of posterior pituitary by muscular contraction, there would have to be enough posterior pituitary to overcome whatever counter-effect the adrenalin would have* [R. 222].

In connection with POINT ONE, *supra*, we have shown that Mason was biased and gave contradictory testimony.

Conclusion.

The judgment of conviction appealed from should be reversed and the case remanded to the District Court with instructions to enter a verdict of not guilty.

Respectfully submitted,

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Los Angeles, California,

January 14, 1948.

No. 11690

IN THE

United States Circuit Court of Appeals

FOR THE NINTH CIRCUIT

PASADENA RESEARCH LABORATORIES, INC., a corporation,
and RUSSELL R. BAVOuset,

Appellants,

vs.

UNITED STATES OF AMERICA,

Appellee.

APPELLEE'S BRIEF.

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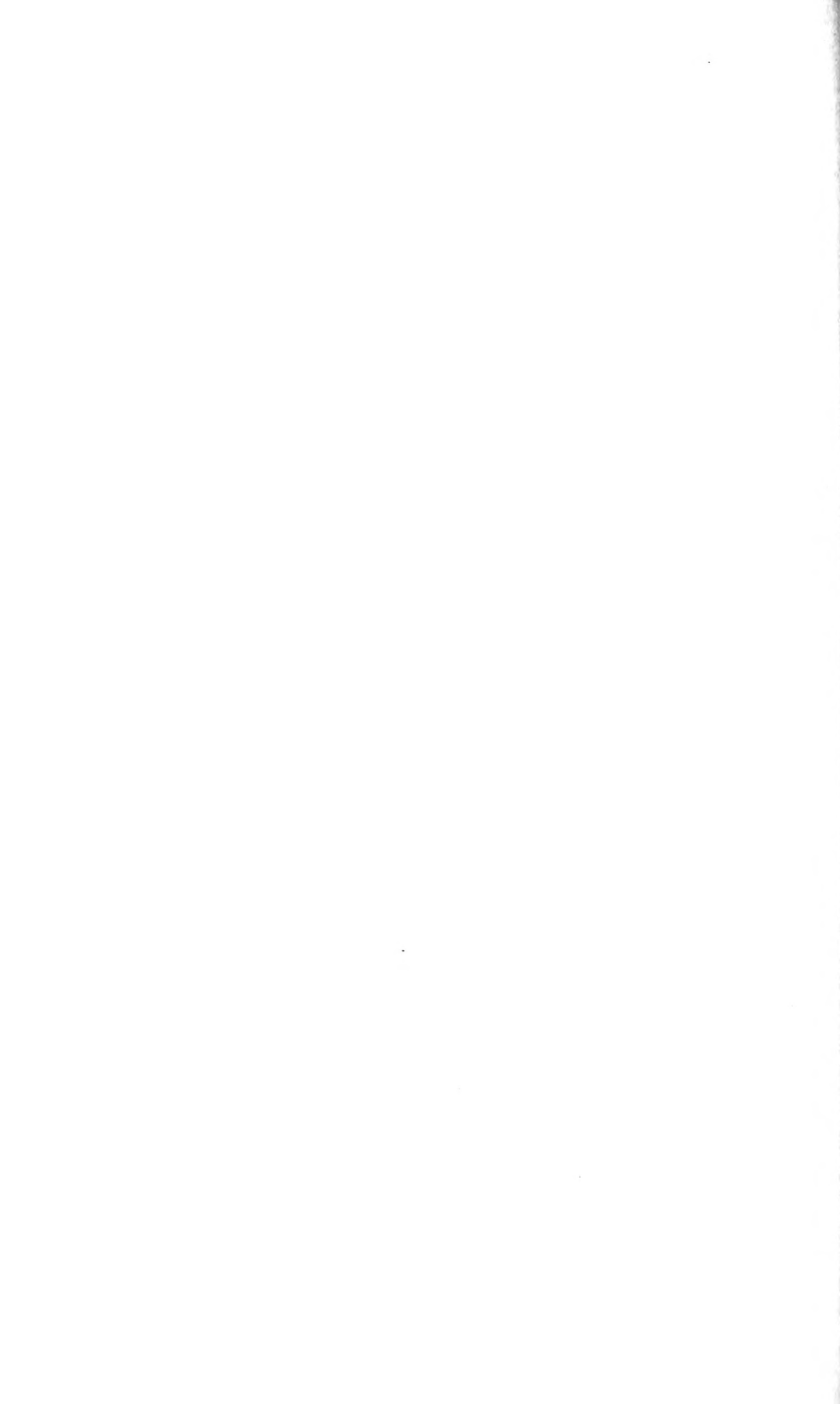
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No. 11690
IN THE
United States Circuit Court of Appeals
FOR THE NINTH CIRCUIT

PASADENA RESEARCH LABORATORIES, INC., a corporation,
and RUSSELL R. BAVOuset,

Appellants,

vs.

UNITED STATES OF AMERICA,

Appellee.

APPELLEE'S BRIEF.

I.

STATEMENT OF JURISDICTION.

Pursuant to Title 21, U. S. C., Section 331(a) and 333(a), as well as Title 28, U. S. C., Section 41(2), the District Court had jurisdiction to try the defendants.

Under Title 28, U. S. C., Sections 225(a) and (d), this court has authority to review the judgment of the District Court.

II.

STATEMENT OF THE FACTS.

The Information filed in this case charges the defendants in seven counts with violations of the Federal Food, Drug and Cosmetic Act, resulting from the interstate shipment of drugs that were adulterated and misbranded.

After trial without a jury [R. 17], the District Court found both defendants, Appellants here, guilty as to Counts I, II, III, IV and VII, but not guilty as to Counts V and VI.

While defendants were convicted on five counts, sentence was imposed as for three offenses [R. 20]. Counts I and II involve the same product, the same shipment and the same evidence, the only difference being that in Count I, the product is charged with being adulterated, while in Count II, the product is charged with being misbranded. A parallel situation exists between Counts III and IV. Count VII stands alone.

A. Sterile Indoform.

[Counts I and II, Exhibits 3, 4 and 5.]

The Information charges, in Count I, that when this drug "Sterile Indoform" was introduced into interstate commerce, it was adulterated within the meaning of Title 21, U. S. C., Section 351(c) since its strength differed from what it purported and was represented to possess [R. 2-3]. The label declares the presence of *three* International Units of *posterior pituitary* and *one grain* of *thyroid substance*; whereas, the Government contended the drug contained a lesser amount of posterior pituitary and no thyroid substance. We submit the evidence fully supported this contention.

Count II charges that the "Indoform" was misbranded within the meaning of Title 21, U. S. C., Section 352(a), in that the label statements with respect to the presence of posterior pituitary and thyroid substance are false and misleading [R. 4-5].

By stipulation [R. 14], it was admitted that defendants shipped a number of vials containing the product "Indoform" in interstate commerce on or about September 17, 1945, from Pasadena, California, to Dr. Joseph C. Bunten, Cheyenne, Wyoming, labeled as described in Counts I and II. It was also stipulated that on or about January 24, 1946, Food and Drug Inspector Davidson collected a sample of this shipment from Dr. Bunten, consisting of one vial and contents. After sealing this sample with an official seal, properly identified, Inspector Davidson forwarded the sample by United States Mail to the Pharmacology Division, Food and Drug Administration, Washington, D. C.

Before outlining the Government's evidence as to the adulterated and misbranded condition of this "Indoform," it is highly pertinent to note that the appellant Russell R. Bavouset admitted the Government's contention with respect to *posterior pituitary*—namely, that this shipment of "Indoform" contained such small quantities of posterior pituitary as to be immeasurable [R. 143-4]. This admission was based upon an independent test conducted by the Cooper Laboratories at defendants' behest, after the shipment was made.

The Government's affirmative evidence with respect to the deficiencies in "Indoform," as to posterior pituitary, stems from the testimony of Arnold E. Mason. Mr. Mason had been employed with the Food and Drug Administration as a pharmacologist and analyst, though at the time of trial he testified he was then employed as a pharmacologist with Crystal (Bristol) Laboratories, Syracuse, New York [R. 57].

On February 18, 1946, while still with the Food and Drug Administration, Washington, D. C., Mr. Mason

analyzed the sample of "Indoform" which Inspector Davidson had collected, to determine the presence of posterior pituitary. His method of analysis was that prescribed by the United States Pharmacopoeia [R. 80]. In his testimony, Mr. Mason gave a detailed description of the method he used [R. 60-73, 80-84, 215-225].

Mr. Mason found that the "Indoform" he examined contained practically no posterior pituitary; if it contained any at all, the amount was immeasurable [R. 59, 74].

Mr. Mason also testified that posterior pituitary is very stable except at excessively high temperatures; it would break down if it were boiled at 212° Fahrenheit for five or six hours [R. 73-74]. Otherwise, it would remain stable and continue its effectiveness for many months, and even years [R. 74].

Mr. Mason expressed the opinion that on the date defendants shipped the product "Indoform" interstate, September 17, 1945—five months before his analysis, it could *not* have contained three units of posterior pituitary per cubic centimeter; and stated that on that date, if the product contained any posterior pituitary at all, it was an immeasurable quantity [R. 75-76].

The label of the product "Indoform" contains no cautionary statement prescribing a particular mode of storage [Govt's Ex. 4, R. 63].

Mr. Mason further testified that when he received the sample of "Indoform" [Govt's Ex. 3], the vial was full and the rubber stopper or cork was protected with a celluloid seal *around* it; and that it appeared as if it had never been opened [R. 215, 79-80].

Appellants' witness, Dr. Icke, who is employed as director of research at the Pasadena Research Laboratories,

testified that one of the ingredients of "Indoform," suprarenal cortex extract, contains adrenalin which would interfere with the test for posterior pituitary so that the latter ingredient would not be as active as it would if the adrenalin were not present [R. 179-181].

In rebuttal, Mr. Mason testified that the cortex might contain very small amounts of adrenalin [R. 216]. Such minute amounts would be destroyed in the course of the test he made [R. 225]. Mr. Mason stated the test he conducted is just as accurate as if there were no suprarenal cortex present [R. 217]. He stated he has conducted many similar tests upon other preparations of the same nature, which included suprarenal cortex, and was able to establish the presence of the amount of posterior pituitary claimed [R. 217].

A significant fact with respect to the test conducted by Mr. Mason is that he used the "Indoform" in full strength [R. 73], whereas the standard solution against which he tested the "Indoform" was diluted fifty times [R. 72]. Also, the standard solution was made from a preparation containing *two* units of posterior pituitary per cc., whereas the "Indoform" here involved was labeled to contain *three* units per cc. [R. 72]. Thus, if the "Indoform" contained the declared amount of posterior pituitary, it would have been over fifty times as strong as the standard solution [R. 73]. Nevertheless, the "Indoform" did not give a reaction in the test showing even a measurable amount of posterior pituitary [R. 73, 83-4].

Mr. Mason did not add anything to the vial of "Indoform" or tamper with its contents [R. 77]. After conducting his tests, he sent the vial to San Francisco for further analysis [R. 77].

Mr. Buell, a chemist of the Food and Drug Administration at San Francisco, received the vial of "Indoform" transmitted from Mr. Mason. On March 27, 1946, he analyzed this product for its *thyroid* content, as indicated by the presence of organically combined iodine [R. 87]. The label of the product declares the presence of "Thyroid Substance 1 gr." [R. 63]. Mr. Buell found no organically combined iodine at all [R. 89].

Mr. Buell testified that the label statement "Thyroid Substance 1 gr." means that the product contains one grain of the active constituent of the thyroid as organically combined iodine [R. 89]. Buell stated that thyroid is extremely stable [R. 89-90]. When defendants shipped the "Indoform" interstate it did not, in Mr. Buell's opinion, contain thyroid substance present as organically combined iodine [R. 90].

The United States Pharmacopoeia defines and describes "thyroid" as follows [R. 136-7]:

"Thyroid is the cleaned, dried and powdered thyroid gland previously deprived of connective tissue and fat.

* * * * *

"It is obtained from domesticated animals that are used for food by man. *Thyroid contains not less than 0.17 per cent and not more than 0.23 per cent of iodine in thyroid combination*, and must be free from iodine in inorganic or any form of combination other than peculiar to the thyroid gland."

Appellants admitted that "Indoform" contains no organically combined iodine [R. 110], but contended that the product does not purport to contain such iodine by

reason of the disclaimer on the label [R. 111]. The label disclaimer reads [R. 63]:

“This preparation does not contain any known therapeutically useful constituent.”

Appellants assert that the product contains a water extract of desiccated thyroid not including its iodine content [R. 111]. Appellant Bavouset, manager of the Research Laboratories, stated he did not know the type of material that is designated by the term “thyroid substance” as used on the label [R. 111].

Despite the disclaimer on the label, Mr. Bavouset admitted that posterior pituitary and whole ovarian, which are other ingredients of “Indoform” [R. 63], do have therapeutic value [R. 135].

B. Sterile Solution Pluri-B.

[Counts III and IV, Exhibits 6 and 7.]

The Information charges in Count III that when this product, “Pluri-B,” was introduced into interstate commerce it was adulterated within the meaning of Title 21, U. S. C., Section 351(c), since its strength differed from what it purported and was represented to possess [R. 5-6]. The label declares the presence of *50 milligrams of thiamine hydrochloride in each cubic centimeter*, whereas the Government contended the drug contained a lesser amount of thiamine hydrochloride.

The Government’s proof indicated that the product contained but 33 milligrams rather than 50 milligrams.

Count IV charges that the "Pluri-B" was misbranded within the meaning of Title 21, U. S. C., Section 352(a), in that the label statements with respect to the presence of thiamine hydrochloride are false and misleading [R. 7-8].

By stipulation [R. 15], it was admitted that appellants shipped a number of vials containing the product "Pluri-B" in interstate commerce on or about July 16, 1945, from Pasadena, California, to Dr. Clement Swain, Reno, Nevada, labeled as described in Counts III and IV. It was also stipulated that on or about August 30, 1945, Food and Drug Inspector Griebeling obtained a sample of this shipment from Dr. Swain, consisting of two vials and contents. After sealing this sample with an official seal, properly identified, Inspector Griebeling forwarded the sample by United States Mail to the Vitamin Division, Food and Drug Administration, Washington, D. C.

Dr. Tolle, Assistant Chief of the Vitamin Division of the Food and Drug Administration, among his other duties, is charged with the receipt and distribution of samples for analysis [R. 212]. When he received the vial identified as Government's Exhibit 6 "*Pluri-B*," he observed that the vial appeared to be full and appeared not to have been tampered with [R. 212]. Dr. Tolle stated it is the practice of the Administration to have its inspectors note on their collection reports that a sample has been opened, if it has been; in such event, Dr. Tolle would not have had the sample analyzed in his laboratory [R. 213].

Mr. Capps, a chemist in the Vitamin Division, testified that on September 24, 1945, he examined the vial of "Pluri-B" identified as Exhibit 6 [R. 99]. While the label declares the presence of 50 milligrams of thiamine hydrochloride per cc., his examination showed that the drug contained 33 milligrams of thiamine hydrochloride per cc. [R. 99-100]. In making this examination, he followed the thiocrome procedure for thiamine described in the United States Pharmacopoeia [R. 98-99]. The record shows the details of this procedure [R. 101-106].

Chemist Capps stated that in a properly made solution, thiamine hydrochloride is stable except when exposed to extremely high temperatures [R. 100]. Appellant Bavouset testified that it was in a proper acid base and would substantially retain its potency for a year [R. 131, 149, 151]. Bavouset further stated that their products are all bottled and sealed in accordance with the most improved methods, designed (1) to prevent impurities from getting in; (2) to protect the contents from light; and (3) to keep the contents in a reasonably good state of preservation [R. 131-132].

In chemist Capp's opinion, the vial of "Pluri-B" which he examined did not contain more than 33 milligrams of thiamine hydrochloride per cc. when it was shipped interstate on July 16, 1945, less than two months before he analyzed it [R. 100-101].

Mr. Bavouset admitted that at the time this drug was shipped his laboratory did not have the equipment to make the thiocrome determination for thiamine [R. 144].

C. Sterile Solution Pluri-B.

[Count VII, Exhibits 1 and 2.]

The Information charges in Count VII that when this product, another type of "Pluri-B" was introduced into interstate commerce it was adulterated within the meaning of Title 21, U. S. C., Section 351(c), since its purity and quality fell below that which it purported and was represented to possess [R. 10-12]. Thus the drug was represented as suitable for intramuscular and intravenous use, a use which requires the product to be free from undissolved material, whereas the Government contended and proved that this drug contained *undissolved material*.

By stipulation [R. 16], it was admitted that appellants shipped a number of vials containing the product "Pluri-B" in interstate commerce on or about June 18, 1946, from Pasadena, California, to Dr. P. M. Ryerson, Phoenix, Arizona, labeled as described in Count VII. It was also stipulated that on or about July 12, 1946, Food and Drug Inspector Kerr collected a sample of this shipment from Dr. Ryerson, consisting of six vials and contents. After sealing this sample with official seals properly identified, Inspector Kerr forwarded it by Railway Express to the Pharmacology Division, Food and Drug Administration, Washington, D. C.

Dr. Wiley, Chief of the Chemical Section, Medical Division, Food and Drug Administration, Washington, D. C., with specialized training in biochemistry, testified that he received this sample "Pluri-B" on July 23, 1946, and

examined it on August 1, 1946 [R. 33, 38]. Dr. Wiley stated that all of the vials in the sample were sealed, capped and full when he received same [R. 226].

On examination, Dr. Wiley found that all six vials in the sample were very badly contaminated with undissolved material; that is, they contained a considerable quantity of material which was not in solution and was visible with the naked eye [R. 34].

The amount of undissolved material in the vials was the same on the date of Dr. Wiley's testimony, June 17, 1947, as on the day he first examined the sample, August 1, 1946 [R. 37-38]. In his opinion, the undissolved material was present on June 18, 1946, the date when appellants shipped this "Pluri-B" interstate [R. 42].

The label of the product contains no statement as to the conditions under which it should be stored [R. 43].

Only such an improbable factor as transmitting the sample to Washington in a refrigerator car might have hastened the crystallization, if it had not already taken place [R. 42].

Dr. Wiley testified that the presence of the noted undissolved materials in the vials was caused by a super-saturated solution of riboflavin [R. 44]. He stated that in the product there was about twenty times as much riboflavin as may ordinarily be dissolved in a water solution [R. 46]. Riboflavin is stable and would remain in solution if the amount dissolved is below the saturation point [R. 44].

Mr. Bavouset testified that the undissolved material present was a precipitate of riboflavin, and that very often in such a case, putting the product in warm water would cause the riboflavin to go back into solution [R. 145]. He also stated that in his opinion nothing had been added to the vials in Exhibit 1, 'Pluri-B,' other than what he had put into them [R. 146].

Dr. Icke, appellants' witness, testified that the undissolved particles in Government's Exhibit 1, should dissolve if the vial were put in lukewarm water with a temperature of 110°—120° Fahrenheit [R. 190].

In rebuttal, Dr. Wiley testified that in the course of his examination of this sample, he had placed the vials in warm water of about 150° Fahrenheit for 10-15 minutes; at the end of that time the undissolved material was still present [R. 226-227].

Dr. Clinton H. Thienes, medical doctor and pharmacologist, testified to the dangers inherent in a "sterile solution" which is intended for intravenous or intramuscular injection and which contains undissolved particles; such a product may cause blockage of circulation, shock, pain and infection [R. 49-50]. Dr. Thienes stated that it is the consensus of practitioners that such solutions must be free from undissolved particles [R. 50]. This is the view also expressed in the United States Pharmacopoeia [R. 50]. In the opinion of Dr. Thienes, the contents of the vials in Government's Exhibit 1, do not meet the standards for a sterile solution intended for intramuscular and intravenous use [R. 51].

III.

STATUTORY PROVISIONS INVOLVED.

Federal Food, Drug and Cosmetic Act.

“*Section 201.* Definitions; generally. [21 U. S. C. 321.]

“For the purposes of this chapter—

- (n) If an article is alleged to be misbranded because the labeling is misleading, then in determining whether the labeling is misleading there shall be taken into account (among other things) not only representations made or suggested by statement, word, design, device, or any combination thereof, but also the extent to which the labeling fails to reveal facts material in the light of such representations or material with respect to consequences which may result from the use of the article to which the labeling relates under the conditions of use prescribed in the labeling thereof or under such conditions of use as are customary or usual.”

“*Section 301.* Prohibited acts. [21 U. S. C. 331.]

“The following acts and the causing thereof are hereby prohibited:

- (a) The introduction or delivery for introduction into interstate commerce of any food, drug, device, or cosmetic that is adulterated or misbranded.”

“*Section 303.* Penalties—Violation of Sec. 301. [21 U. S. C. 333.]

- (a) Any person who violates any of the provisions of Section 301 shall be guilty of a misdemeanor and shall on conviction thereof be subject to

imprisonment for not more than one year, or a fine of not more than \$1,000, or both such imprisonment and fine * * *.”

“*Section 501.* Adulterated drugs and devices. [21 U. S. C. 351.]

“A drug or device shall be deemed to be adulterated—

- (c) If it is not subject to the provisions of paragraph (b) of this section and its strength differs from, or its purity or quality falls below, that which it purports or is represented to possess.”

“*Section 502.* Misbranded Drugs and devices. [21 U. S. C. 352.]

“A drug or device shall be deemed to be misbranded—

- (a) If its labeling is false or misleading in any particular.”

IV.

QUESTIONS INVOLVED.

It appears from the contentions in Appellants' brief that the following questions are presented by this appeal:

(1) Is there substantial evidence to support the District Court's conclusion that the products involved were adulterated or misbranded when the appellants introduced them into interstate commerce?

(2) Was there prejudicial error in the hypothetical questions which the Government's witnesses were permitted to answer?

V.

SUMMARY OF ARGUMENT.

A. The District Court's Judgments of Conviction
Are Supported by Substantial Evidence.

The Government's burden was to prove its case beyond a reasonable doubt, not beyond all doubt.

The products involved in this case were very stable in themselves and were packaged, corked and sealed in a manner best designed to preserve such integrity as they had when they were manufactured.

Appellants shipped these products to doctors in the regular course of business. Government inspectors obtained a portion of each of these shipments from the doctors and sent them in the regular course of business to Food and Drug Administration laboratories in Washington, D. C. Upon receipt by the Government's chemists the products were full, sealed and apparently untampered with.

Only such highly unusual and improbable circumstances as boiling for five or six hours, or freezing, or adding additional ingredients could have affected the contents of the products.

The Government does not have to exclude all possibility that the products may have been tampered with. Whether these products actually were tampered with or substantially changed *after* their interstate shipment was a question of fact for the court sitting without a jury.

The products were therefore in substantially the same condition when received and analyzed by the chemists as they had been when appellants shipped them interstate, a relatively short time before.

Appellants admit that the "Indoform" (Counts I and II) contained practically no posterior pituitary, though the label declares the presence of 3 units per cc. The Government's chemist affirmatively established that either there was no posterior pituitary present or it was present in such small amounts as to be immeasurable.

The thyroid substance which the "Indoform" label declared to be present in the product signifies the *active constituent* of the thyroid, which is organically combined iodine [R. 89]. No organically combined iodine was found in the product, on analysis.

Appellants admitted there was no iodine present but contended that doctors were informed of this fact by the label disclaimer—"This preparation does not contain any known therapeutically useful constituent." This label is misleading (1) because other constituents in the product admittedly *do have* therapeutic value, and (2) there is no clear-cut statement that this particular thyroid substance does not contain the iodine constituent.

Uncontradicted evidence as to the product "Pluri-B" (Counts III and IV) established that it contained only 33 milligrams of thiamine hydrochloride per cc., though the label declares the presence of 50 milligrams. Defendants admitted that at the time they shipped this product

they did not have the equipment necessary to test the product and actually did not test it [R. 141, 144].

Manufacturers of drugs have a serious responsibility to the public to maintain controls necessary to secure the purity, potency and safety of their products.

Uncontradicted evidence as to the other shipment of "Pluri-B" (Count VII), established that it was badly contaminated with undissolved material visible to the naked eye. Such material is a menace to health in a product that is offered as a sterile solution for intramuscular or intravenous use.

B. No Error Was Committed by the District Court in Permitting The Government's Witnesses to Answer Hypothetical Questions.

In a criminal case which is tried by the court without a jury, it is assumed that the trial court considered only competent and material evidence. In such a case, the reception of incompetent evidence is not prejudicial.

However, even if there had been a jury trial, the questions were proper.

First, the evidence directly, fairly and reasonably tended to establish all of the facts assumed in each hypothetical question.

Second, the Government's experts gave their opinions not on any *ultimate* issues of fact but only with respect to those subsidiary issues of fact where their opinions were a proper aid to the court sitting without a jury.

VI.
ARGUMENT.

A. The Government's Burden Was to Prove the Defendants Guilty Beyond a Reasonable Doubt, But Not Beyond All Doubt; the District Court's Judgments of Conviction Are Supported by Substantial Evidence.

This is a criminal prosecution that was tried by the District Court, defendants having waived jury trial [R. 17]. We do not challenge appellants' assertion that it was incumbent upon the Government to prove its case "beyond a reasonable doubt." However, as appellants interpret this phrase, it means "beyond all doubt."

Such an argument was effectively laid to rest in *Henderson v. United States*, 143 F. (2d) 681 (C. C. A. 9th), where this court stated on page 682:

"The proof in a criminal case need not exclude all doubt. If that were the rule, crime would be punished only by the criminal's own conscience, and organized society would be without defense against the conscienceless criminal and against the weak, the cowardly, and the lazy who would seek to live on their wits. The proof need go no further than reach that degree of probability where the general experience of men suggests that it has passed the mark of reasonable doubt.

"And judges and juries do not begin the solution of the complex problems presented to them from a zero of knowledge. They start with the vast common knowledge and understanding possessed by the people."

At another point, on page 682, the court said:

“It is a familiar principle, which it is our duty to apply, that an appellate court will indulge all reasonable presumptions in support of the rulings of a trial court and therefore that it will draw all inferences permissible from the record, and in determining whether evidence is sufficient to sustain a conviction, will consider the evidence most favorably to the prosecution.”

1. IDENTITY OF THE SAMPLES.

Appellants vigorously argue the proposition that the burden is upon the Government to establish that in reasonable probability the testimony of the Government's witnesses with respect to the condition of the products involved, *as of the date of analysis*, substantially reflects the condition of those products *as of the date defendants shipped them interstate*. With this proposition we have no quarrel.

Appellants quote from 32 *Corpus Juris Secundum*, Section 607, page 458 (App. Br. 23). One of the sentences omitted from this quotation reads:

“It is unnecessary to show an absence of tampering on the part of every person through whose hands the article has passed; as long as the article can be identified it is immaterial in how many or in whose hands it has been.”

Similarly, appellants quote from *United States v. S. B. Penick & Co.*, 136 F. (2d) 413, 415 (C. C. A. 2nd), (App. Br. 21). From this quotation, also, several sentences are omitted which we supply:

“But there is no hard and fast rule that the prosecution must exclude all possibility that the article

may have been tampered with. See *Lestico v. Kuehner*, 204 Minn. 125, 283 N. W. 122, 125.

“Here the samples were taken in the ordinary course of business for the very purpose of being retained as samples; they were put in the usual place where samples were kept to remove them from accident or meddling and there they remained, so far as appears, undisturbed. We think this showing was sufficient to justify admission in evidence of the bottles and their contents and that it was for the jury to decide how likely it was that some other substance had been substituted for that which was originally put in the bottles. *Pennsylvania R. Co. v. Fox & London*, 93 F. (2d) 669 (C. C. A. 2nd), cert. den. 304 U. S. 566; *Hanify Co. v. Westberg*, 16 F. (2d) 552 (C. C. A. 9th).” (Emphasis supplied.)

In the instant case the Government undertook to establish the identity of the samples *as of the time of shipment*, by circumstantial evidence relating to their interstate shipment, the identity of the consignees and the condition of the drugs when received by the Government chemists, together with the reasonable inferences flowing from such evidence. The Government’s evidence was strengthened by admissions in appellant Bavouset’s testimony, which established (1) that the product “Indoform” was adulterated and misbranded when it was introduced into interstate commerce [R. 143], and (2) that all of the products here involved were likely to have been adulterated and misbranded at that time by reason of the poor manufacturing controls maintained by the appellants [R. 141-144].

Counts I, II, III, IV and VII involve the interstate shipment of three different products consigned to three different doctors. In each of these shipments there were

*a number of vials.*¹ The inference is clear that these shipments were made by the defendants in the regular course of business and so received by the doctors. Defendants clearly expected these products to maintain for a long period of time, whatever stability and integrity they had at the time of shipment. It is hardly conceivable that within a period of a few months, three of their products shipped to different doctors would have been subjected to freezing temperatures, boiling for five or six hours, and the addition of extraneous material.

The products bore no label statements suggesting special conditions of storage. It may reasonably be assumed that the doctors who received such products handled and stored them in the normal way.

Samples consisting of *a portion* of each of these shipments were obtained from the doctor consignees by inspectors of the U. S. Food and Drug Administration. The inspectors shipped the samples to the appropriate laboratories for analysis. Their testimony was deemed unnecessary in view of the stipulation entered into to shorten the trial. From the stipulation it is clear that the work done by the inspectors in connection with the collection and shipment of these samples was done in the regular course of business and in the performance of their official duties. It may be presumed that such official duties were regularly performed. In *United States v. Chemical Foundation, Inc.*, 272 U. S. 1, at pages 14-15, the Supreme Court stated:

“The presumption of regularity supports the official acts of public officers and, in the absence of clear

¹It may be noted that the shipment described in Counts V and VI, with respect to which defendants were found not guilty, consisted of only *one vial* [R. 15-16].

evidence to the contrary, courts presume that they have properly discharged their official duties.”

See, also:

Bowles v. Glick Bros. Lumber Co., 146 F. (2d) 566, at p. 571 (C. C. A. 9th);

Dunn v. Ickes, 115 F. (2d) 36-37 (C. A., D. C.), cert. den. 311 U. S. 698;

Calif. Code of Civ. Proc., Section 1963, Subd. (15).

It was testified by the chemists who analyzed these samples that, on receipt, each of the vials comprising the samples was full, sealed and apparently untampered with. The vials of amber colored glass were capped, sealed and packaged in accordance with the best known methods designed to protect the integrity of the contents. Moreover, it was indisputably established that these products are extremely stable except under such unusual circumstances as boiling for five or six hours, freezing temperatures, addition of extraneous materials to contents, etc. Record references to these facts are fully set forth under the Government's "Statement of the Facts."

When it is considered that the vials in each sample were full, sealed with the manufacturer's seal—with contents apparently untouched when received by the analysts—there stands out in bold relief the futility as well as the staggering burden and expense of summoning officials and employees of the Railway Express Agency, the Post Office Department and the doctors, as well as any other persons who might have had anything to do with these products in the normal course of their interstate shipment. And for what purpose would such witnesses be called? To testify that they did not boil the products for six

hours—that they did not add other ingredients to the products though the products were sealed, capped and full, etc.! As a practical matter most persons who handled the transportation of these products in the regular course of business would have no recollection whatsoever about them, even if it were possible to locate them.

While defendants' witness, Dr. Icke, described fanciful conditions under which these products may have deteriorated subsequent to their interstate shipment, his credibility and the weight to be given his testimony were matters for the trial court, sitting without a jury.

Newman v. United States, 156 F. (2d) 8 (C. C. A. 9th), cert den.;

Cain v. United States, 67 S. Ct. 115.

A significant factor bearing upon the identity of the samples is the comparatively short time that elapsed between their interstate shipment by the defendants and their analysis by Government chemists. The "Pluri-B" involved in Count VII was shipped interstate on June 18, 1946, and was analyzed on August 1, 1946, less than six weeks later. The "Pluri-B" involved in Counts III and IV was shipped interstate on July 16, 1945, and analyzed on September 24, 1945, two months and one week later. The "Indoform" involved in Counts I and II was shipped interstate on September 17, 1945, and analyzed on February 18, 1946, five months later; defendants' admissions with respect to the "Indoform" make the five months lapse of time entirely immaterial, as will be shown shortly.

Also, the stipulation [R. 13-17] establishes that the doctors could have had the shipments in their possession only a short time before the samples were collected by the inspectors.

For these reasons we submit that the Government established beyond a reasonable doubt, if not beyond all doubt, that the samples concerning which the Government's witnesses testified were substantially the same on the date when their analyses were made, as they were at the time when defendants shipped them interstate.

2. ADMISSIONS BY DEFENDANTS AND INDEPENDENT PROOF OF VIOLATIONS.

With respect to the interstate shipment of "Indoform" (Counts I and II), defendant Bavouset, general manager of defendant Pasadena Research Laboratories, admitted that he had had this product independently tested by the Cooper Laboratories, who found it contained such small quantities of posterior pituitary as to be immeasurable [R. 143]. Defendants manufactured between 65 and 100 vials of "Indoform" at a time [R. 133]. The analysis by Cooper Laboratories was made *after* defendants had made the interstate shipment to Dr. Bunten [R. 14, 144]. This is one indication of the laxity of controls maintained by the defendants with respect to a drug to be administered by injection.

At any rate, the admission that the "Indoform" contained such small amounts of posterior pituitary as to be immeasurable is, in itself, enough to sustain the conviction on Counts I and II, since the label declares the presence of 3 units of posterior pituitary per cc. [R. 63]. The testimony of chemist Mason affirmatively and graphically establishes that there was no posterior pituitary present in the "Indoform," or if there was any there at all it was in such small amounts as to be immeasurable [R. 57-84, 215-226]. Posterior pituitary is very stable unless it is

kept at a boiling temperature for five or six hours [R. 73-74].

A second and independent reason for sustaining the conviction as to Counts I and II, is the further admission by defendant Bavouset that the “thyroid substance” which the label declared to be present in the “Indoform” was present in a form from which the potent organically-combined iodine had been removed [R. 110].

The definition of “thyroid” in the United States Pharmacopoeia states that it “contains not less than 0.17 per cent and no more than 0.23 per cent of iodine in thyroid combination” [R. 136-137]. Government witness Buell testified that the label statement, “each cc. contains Thyroid Substance I grain,” means one grain of the active constituent of the thyroid as organically-combined iodine [R. 89]. Mr. Buell analyzed the product and found no thyroid present at all [R. 89]. The iodine in thyroid is extremely stable [R. 89-90].

A colloquy between the court and defendant Bavouset indicates the nebulous and shifty character of defendants’ operations [R. 111-112]:

“The Court: Then this Indoform did not purport to contain any iodine?

The Witness: No, sir.

The Court: What is the thyroid substance here it did purport to contain?

The Witness: Your Honor, I do not know the type of material that is designated therein. We put a disclaimer on the product, stating that it did not contain therapeutically useful constituents to let the doctor know that the thyroid content was not the iodine content.

The Court: In the trade would the term 'thyroid substance' have any particular meaning?

The Witness: In the trade the words 'thyroid substance' for oral administration would mean the whole gland, that is, of course, meant to feed it or made ready for oral administration.

The Court: And that would contain iodine?

The Witness: Yes, your Honor; that would contain iodine.

Q. By Mr. Stick: In an aqueous solution would it contain that? A. No, it would not.

The Court: Is there anything on the label, this Indoform label, to indicate it is an aqueous solution?

The Witness: I do not believe so, your Honor
* * *."

The so-called disclaimer which Mr. Bavouset thought would inform the doctor "that the thyroid content was not the iodine content," reads as follows:

"This preparation does not contain any known therapeutically useful constituent." [R. 63.]

The misleading nature of this disclaimer becomes clearer in the light of Mr. Bavouset's further admission that other constituents of "Indoform" such as posterior pituitary and whole ovarian *do have therapeutic value* [R. 135].

Appellants did not unequivocally state on the label that the "thyroid substance" did not contain any of the iodine constituents which are normally in the thyroid, though he, Bavouset, protests that that was his intention [R. 135]. Actually, the statement of ingredients on the label declares that each cc. contains 1 grain of thyroid substance. This statement is false and misleading as charged

in Count II. In *United States v. 95 Barrels * * * Vinegar*, 265 U. S. 438, the court observed on pages 442-443:

“The statute is plain and direct. Its comprehensive terms condemn every statement, design and device which may mislead or deceive. Deception may result from the use of statements not technically false or which may be literally true. The aim of the statute is to prevent that resulting from indirection and ambiguity, as well as from statements which are false. It is not difficult to choose statements, designs and devices which will not deceive. Those which are ambiguous and liable to mislead should be read favorably to the accomplishment of the purpose of the act.”

Section 201(n) of the Act [21 U. S. C. 321(n)] sets forth statutory criteria useful in striking at half truths in products whose labeling is charged with being misleading. That section reads in part:

“* * * in determining whether the labeling is misleading there shall be taken into account (among other things) not only representations made * * * but also the extent to which the labeling fails to reveal facts material in the light of such representations * * *.”

When a product is represented as containing thyroid substance, the only active constituent of which is its iodine content, we submit that the labeling of the product is misleading when it fails to reveal in definite terms *the material fact* that this particular thyroid substance does not contain the iodine constituent.

An analogous situation arose in *H. N. Heusner & Son v. Federal Trade Commission*, 106 F. (2d) 596 (C. C. A. 3rd). That was a petition to modify an order issued by the Federal Trade Commission to cease and desist from using the word "Havana" on cigars which petitioner manufactured in Pennsylvania, from Pennsylvania tobacco, and which he branded "Havana Smokers." Petitioner sought retention of the word "Havana" to be used with this legend: "Notice. These cigars are made in the United States, and only of United States tobacco." On page 597, the court rejected this argument in terms that are quite appropriate here:

"The difficulty of petitioner's position lies in the fact that the implication of the word 'Havana' is totally false. The purchaser can be guided by either label or legend, but not by both * * *. We doubt if petitioner would accede to a true qualification—'Fake Havana Smokers.'"

With respect to the interstate shipment of "Pluri-B" (Counts III and IV), the uncontradicted evidence is that the sample analyzed by Government witness Capps [Govt. Exhibit 6] contained only 33 milligrams of thiamine hydrochloride per cc. [R. 100], though the label declares the presence of 50 milligrams of thiamine hydrochloride per cc. [R. 107].

When thiamine hydrochloride is put in a properly made solution, it is a stable product unless exposed to extremely high temperatures [R. 100]. Defendant Bavouset testified that the solution of this "Pluri-B" was very acid, which he stated is a proper base for retention of the potency of the product [R. 151]. He informed the court he would not expect the product to have lost its potency even a year after it was made [R. 149]. The label of

the product specifies no particular conditions of storage [R. 107].

Coupled with this affirmative evidence there is the admission by defendant Bavouset that at the time when this shipment was made, the defendants *did not have the equipment necessary to make the thiocrome determination for thiamine* [R. 144], which is prescribed by the United States Pharmacopoeia [R. 199-200]. Defendants in fact did not have assays conducted on any of the finished products here involved with the exception of "Indoform," "because the facilities were not available at that time" [R. 141]; and that one assay, which was made *after* interstate shipment, itself established a violation [R. 143].

We feel, and the courts have recognized, that manufacturers of drugs have a serious responsibility to the public to maintain controls designed to secure the purity, potency and safety of their products. In *United States v. Dotterweich*, 320 U. S. 277, the Supreme Court declared with respect to the Federal Food, Drug and Cosmetic Act:

Page 280.

"The purposes of this legislation thus touch phases of the lives and health of people which, in the circumstances of modern industrialism, are largely beyond self-protection. Regard for these purposes should infuse construction of the legislation if it is to be treated as a working instrument of government and not merely as a collection of English words."

Page 281.

"Such legislation dispenses with the conventional requirement for criminal conduct—awareness of some wrongdoing. In the interest of the larger good it

puts the burden of acting at hazard upon a person otherwise innocent but standing in a responsible relation to a public danger.”

Pages 284-285.

“Hardship there doubtless may be under a statute which thus penalizes the transaction though consciousness of wrongdoing be totally wanting. Balancing relative hardships, Congress has preferred to place it upon those who have at least the opportunity of informing themselves of the existence of conditions imposed for the protection of consumers before sharing in illicit commerce, rather than to throw the hazard on the innocent public who are wholly helpless.”

See, also, *United States v. Parfait Powder Puff Co.*, 163 F. (2d) 1008 (C. C. A. 7th), cert. den. 92 L. Ed. 318. In such matters the public, including doctors, are helpless because they are not in a position to make tests and assays upon the innumerable products flowing through commerce. A major purpose of the Federal Food, Drug and Cosmetic Act is to protect the public health by pinning responsibility upon those who are in the logical position to assume it—*e. g.*, the manufacturers and distributors.

With respect to the other shipment of “Pluri-B” (Count VII), the uncontradicted evidence is that all the vials in the sample examined by Government witness Wiley [Govt’s Exhibit 1] were badly contaminated with undissolved material visible to the naked eye [R. 34]. The label declares that this product is a sterile solution for intramuscular or intravenous use [R. 35].

The standards of the United States Pharmacopoeia for such a product call for its being free from undis-

solved material [R. 50]. Dr. Thienes testified to the harm that could result from injecting such a solution containing undissolved material, intravenously or intramuscularly [R. 49-50].

The presence of the undissolved material was caused by the fact that the product contained more riboflavin than could be dissolved in that amount of fluid; the solution was supersaturated [R. 44]. After examining the vials comprising Government's Exhibit 1, appellant Bavouset stated that nothing had been added to them other than what he had put into them [R. 146].

Appellants' witness, Dr. Icke, stated that by exercising careful simple controls, a manufacturer could be certain to detect the presence of supersaturated solutions of riboflavin [R. 192]. He also testified that in his opinion, the undissolved particles in Government's Exhibit 1 would dissolve if the vials were placed in warm or lukewarm water [R. 190].

Government's witness, Dr. Wiley, stated in rebuttal that as a matter of routine laboratory procedure, he placed these vials in warm water of about 150° Fahrenheit and kept them there for ten to fifteen minutes, at the end of which time the undissolved material was still there [R. 226-227].

The court, in comparing the "Pluri-B" involved in Counts III and IV, with the "Pluri-B" involved in Count VII, noted that the label of the first declared the presence of only one milligram of riboflavin per cc. [R. 107], while

the label of the second declared the presence of two milligrams of riboflavin per cc. [R. 35]. In questioning defendant Bavouset about these two products the court brought out the testimony that the "Pluri-B" with one milligram of riboflavin per cc. is just as efficacious as the "Pluri-B" with two [R. 149]. Also, since there is danger of precipitation of riboflavin, it would be a safer product with less riboflavin in it [R. 149].

The following is taken from page 147 of the Record:

"The Court: Is there some definite purpose in including in one of the Pluri-B products only one milligram of riboflavin per cubic centimeter and, in the other, two milligrams?

The Witness: Yes, your Honor. The intramuscular, as I said, it was quite stable and we had a lot of success with it. And then we put in two milligrams. *Perhaps I was a little optimistic*, I don't know, and we had a great deal of good fortune with that at all times, and *upon a very rare occasion something like this did happen.*" (Emphasis supplied.)

The District Court could well question this blithe optimism with respect to a product that could be dangerous to persons in whom it might be injected.

We submit that there was clearly substantial evidence to support the District Court's finding that each of the products involved in this appeal was adulterated and misbranded as charged in the Information.

B. No Error Was Committed by the District Court In Permitting the Government's Witnesses to Answer Hypothetical Questions.

In our understanding of the law, Appellants' entire argument with respect to hypothetical questions is immaterial since this case was tried without a jury [R. 17].

The rule is well established that in a criminal case which is tried by the court without a jury, it is assumed that the trial court considered only competent and material evidence; consequently, the reception of incompetent evidence is not prejudicial. In *Hoffman v. United States*, 87 F. (2d) 410 (C. C. A. 9th), this court stated at page 411:

"This case was tried by the judge and presumably he would consider only material and competent testimony."

And in *Gates v. United States*, 122 F. (2d) 571 (C. C. A. 10th), cert. den. 314 U. S. 698, the court said on page 578, citing the *Hoffman* case and others:

"Where a case is tried to the court without a jury, it is assumed that the court considered only competent and material evidence, and disregarded incompetent, immaterial and improper evidence."

See also:

Daniel v. United States, 127 F. (2d) 1 (C. C. A. 8th), cert. den. 317 U. S. 641;

United States v. David, 107 F. (2d) 519 (C. C. A. 7th).

We do not concede, however, that the questions asked would have been improper in any respect even if there had been a jury trial.

First, we submit that the evidence directly, fairly and reasonably tended to establish all of the facts assumed in each hypothetical question within the requirements laid down by this court in *Travelers Ins. Co. v. Drake*, 89 F. (2d) 47, 50 (C. C. A. 9th). Essentially, our argument on this point would be the same as that already made in Part "A," subdivision "1" of this argument, namely, that the shipments were all made in the regular course of business and it could reasonably be inferred from the evidence that none of the persons in any way connected with the products had boiled them, frozen them or added other ingredients to them. Any other inference would be unreasonable in view of the intact condition of the products when received by the analysts, and in view of the common understanding of conditions that prevail (1) in the regular course of interstate shipment, (2) in the offices of doctors who purchase products for use in treating their patients, and (3) in the collection and handling of official samples taken pursuant to the Federal Food, Drug and Cosmetic Act.

Second, we believe that Appellants' Brief (p. 33) does not correctly state the law with respect to the scope of hypothetical questions that may properly be propounded to expert witnesses.

It is fundamental that the scope and fairness of a hypothetical question are matters resting largely in the discretion of the trial court.

United States v. Aspinwall, 96 F. (2d) 867, 869 (C. C. A. 9th).

See also—

Moyer v. Aetna Life Ins. Co., 126 F. (2d) 141,
144 (C. C. A. 3rd).

Even—

“* * * where a witness answers a hypothetical question not founded on all the facts of the case, the defect goes not to the competency of the evidence but merely affects its weight.”

Permanente Metals Corp. v. Pista, 154 F. (2d)
568, 569 (C. C. A. 9th).

See also—

Forsyth v. Doolittle, 120 U. S. 73, 74;

United States v. Johnson, 319 U. S. 503, 519.

We submit that these cases support the proposition that the interrogating counsel may properly assume any state of facts reasonably supported by the evidence, and may limit those facts within limits permitted in the discretion of the trial court.

Appellants cite *United States v. Spaulding*, 293 U. S. 498 (App. Br. 33), and other cases involving war risk insurance policies in support of the proposition that experts may not state their opinions with respect to the ultimate issues of fact. In the *Spaulding* case, the ultimate issue of fact was whether the respondent was suffering from “total permanent disability,” *as those words are used in the policy and statute authorizing the insurance*. The court said (p. 506):

“* * * that question is not to be resolved by opinion evidence. It was the ultimate issue to be decided by the jury upon all the evidence in obedience to the judge’s instructions as to the meaning of the crucial phrase and other questions of law.”

Similar rulings were made in the other cases cited by appellants, namely, that the experts could not testify that the insurance claimants were *totally and permanently disabled*.

These rulings, we submit, have no bearing on the instant case since none of the questions asked of the experts elicited opinions with respect to the ultimate issues of fact. What are the ultimate issues in this case? They are found in the Information, which reflects the statutory language—were these products *adulterated* or *misbranded* when defendants introduced them into interstate commerce? These issues may be further broken down in the statutory language as follows:

- (1) Was the “Indoform” adulterated in that its strength differed from that which it purported or was represented to possess? (Count I).
- (2) Was the “Indoform” misbranded in that the statements displayed on the vials of said drug were false or misleading? (Count II).
- (3) Was the “Pluri-B” adulterated in that its strength differed from that which it purported or was represented to possess? (Count III).
- (4) Was the “Pluri-B” misbranded in that a statement displayed on the vials of said drug was false or misleading? (Count IV).
- (5) Was the “Pluri-B” adulterated in that its purity or quality fell below that which it purported or was represented to possess? (Count VII).

The Record shows that no expert witness called by the Government gave an opinion with respect to any of these ultimate issues of fact. Nor do the hypothetical questions

which appellants are attacking (App. Br. 26), include any attempt to elicit an opinion as to such ultimate issues. No expert witness testified that in his opinion a product here involved was adulterated when it was introduced into interstate commerce, or that its purity and quality fell below that which it purported and was represented to possess. Instead, the witnesses testified, for example, that the undissolved material was undoubtedly present on June 18, 1946, when it was shipped [R. 41-42].

Of course, the testimony of the Government's experts was related to the issues of fact; otherwise it would have been immaterial. But the opinions they gave were not determinative of the ultimate issues. Thus they in no way infringed upon the function of the trier of the facts to decide whether the "Indoform" was "adulterated when introduced into interstate commerce, in that its strength differed from that which it purported or was represented to possess." The meaning of this statutory language was not interpreted by the experts or applied by them to the facts of the case. Whether undissolved material was present at a certain date was a subsidiary issue of fact, concerning which a qualified expert could properly express an opinion.

In *Transportation Line v. Hope*, 95 U. S. 297, the court said on page 298:

"It is not an objection * * * that he was asked a question involving the point to be decided by the jury. As an expert he could properly aid the jury by such evidence."

And in *Travelers Ins. Co. v. Drake*, 89 F. (2d) 47 (C. C. A. 9th), this court upheld the admission of a doctor's evidence on the cause of a death, observing on page 49:

"While the jury is the sole judge of the facts as to the issue of death and cause of death, that does not, however, make objectionable the opinion of a medical expert in aid to the jury to find the ultimate fact."

See, also—

Cropper v. Titanium Pigment Co., 47 F. (2d) 1038 (C. C. A. 8th), 78 A. L. R. 737, 755;

Francis v. Southern Pac. Co., 162 F. (2d) 813, 817 (C. C. A. 10th);

United States Smelting Co. v. Parry, 166 Fed. 407, 410-415 (C. C. A. 8th).

In litigation under the Federal Food, Drug and Cosmetic Act, the propriety of eliciting expert opinions with respect to such factual issues as the therapeutic efficacy of a drug in the treatment of the ailments for which it is offered, is frequently challenged. Invariably such objections are overruled.

Kar-Ru Chemical Co. v. United States, 264 Fed. 921, 928 (C. C. A. 9th);

*Eleven Gross Packages * * * Dr. Williams' Pink Pills v. United States*, 233 Fed. 71, 73 (C. C. A. 3rd);

United States v. One Device, intended for use as a Colonic Irrigator, 160 F. (2d) 194, 199 (C. C. A. 10th).

One sentence in *United States v. 7 Jugs* * * * *Dr. Salbury's Rakes*, 53 Fed. Supp. 746 (D. Minn.), sums up the rationale for these rulings:

Page 760.

"All of the opinion evidence given by the Government's experts necessarily involved the use of their experience and training on matters of special knowledge not within the grasp of the untutored."

C. Miscellaneous Points.

Appellants contend that certain statements made by Government witness Mason are contradictory and that he was biased (App. Br. 19). Such assertions are not borne out by the Record.

Mr. Mason, who at the time of his testimony was no longer employed with the Food and Drug Administration [R. 57], was particularly meticulous in describing precisely what he had done in the course of his analysis of appellants' product "Indoform," and what he had observed with respect to it [R. 57-84, 215-225].

The following is quoted from the Record, pages 78-80, with respect to the "Indoform," Exhibit 3 (the witness being Mr. Mason):

"The Court: Was that cork sealed *into* the bottle in any way?

The Witness: I do not remember whether it was sealed *into* the bottle or not. It has the same type of rubber stopper that is commonly on such preparations.

* * * * *

The Court: Was the bottle, Exhibit 3, at the time you received it corked or closed and sealed in the same manner or a similar manner [as Exhibit 1]?

The Witness: It was sealed in the same manner as Exhibit No. 1.

Q. * * * * *

A. The rubber cork goes down into the neck of the bottle for a short distance, folds around the outside of the bottle, then is sealed with a plastic seal.

* * * * *

The Court: Did this Exhibit 3, when you received it, the bottle, appear to be so corked?

The Witness: Yes, sir.

The Court: As counsel has just described it?

The Witness: Yes, sir.

The Court: That is, corked and sealed?

The Witness: Corked and sealed.

* * * * *

The Court: Now did this bottle, Exhibit 3, at the time you first saw it appear to be corked and sealed in the same manner as defendants' 'A' for identification?

The Witness: In the same or similar manner."

It is quite clear, from this series of questions and answers, that Mr. Mason testified the product he received was corked and sealed with a plastic seal. It is not certain just what the court meant in the first question quoted above, when it asked whether the cork was sealed *into* the bottle. The witness didn't know whether it was sealed *into* the bottle, but he did know that the bottle was sealed on the *outside*. Consequently, when he testified on rebuttal that "the vial was full and the rubber stopper or cork was protected with a celluloid seal around it when I received it; it appeared as if it had never been opened" [R. 215]—he was merely clarifying statements he had already made. The Record, we submit, does not justify the distorted conclusions drawn by appellants.

VII.
CONCLUSION.

The convictions as adjudged by the court were supported by clear and substantial evidence, enhanced by appellants' admissions as to laxity in the maintenance of manufacturing controls.

We submit that the judgments of the District Court should in all respects be affirmed.

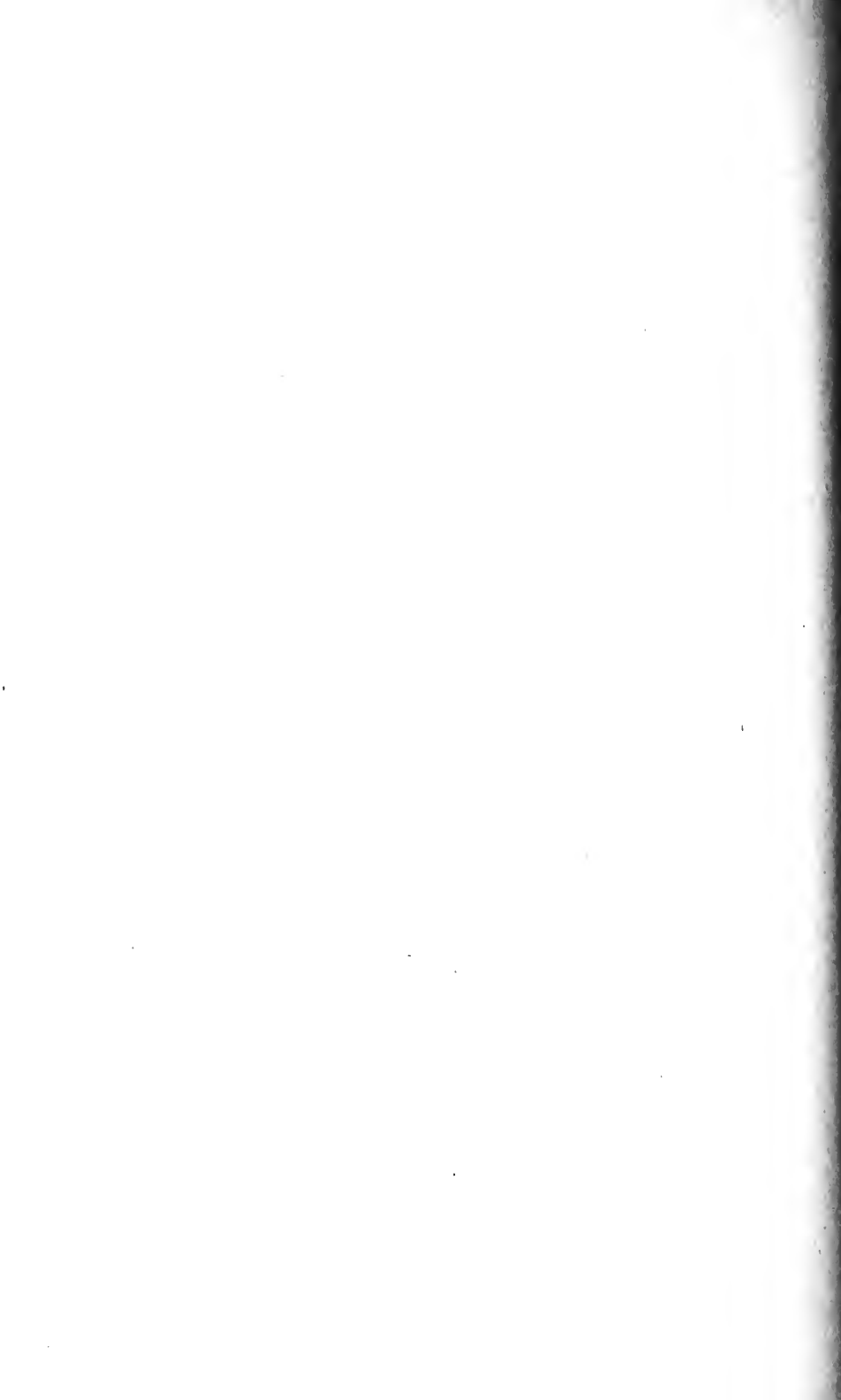
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vs.

UNITED STATES OF AMERICA,

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APPELLANTS' REPLY BRIEF.

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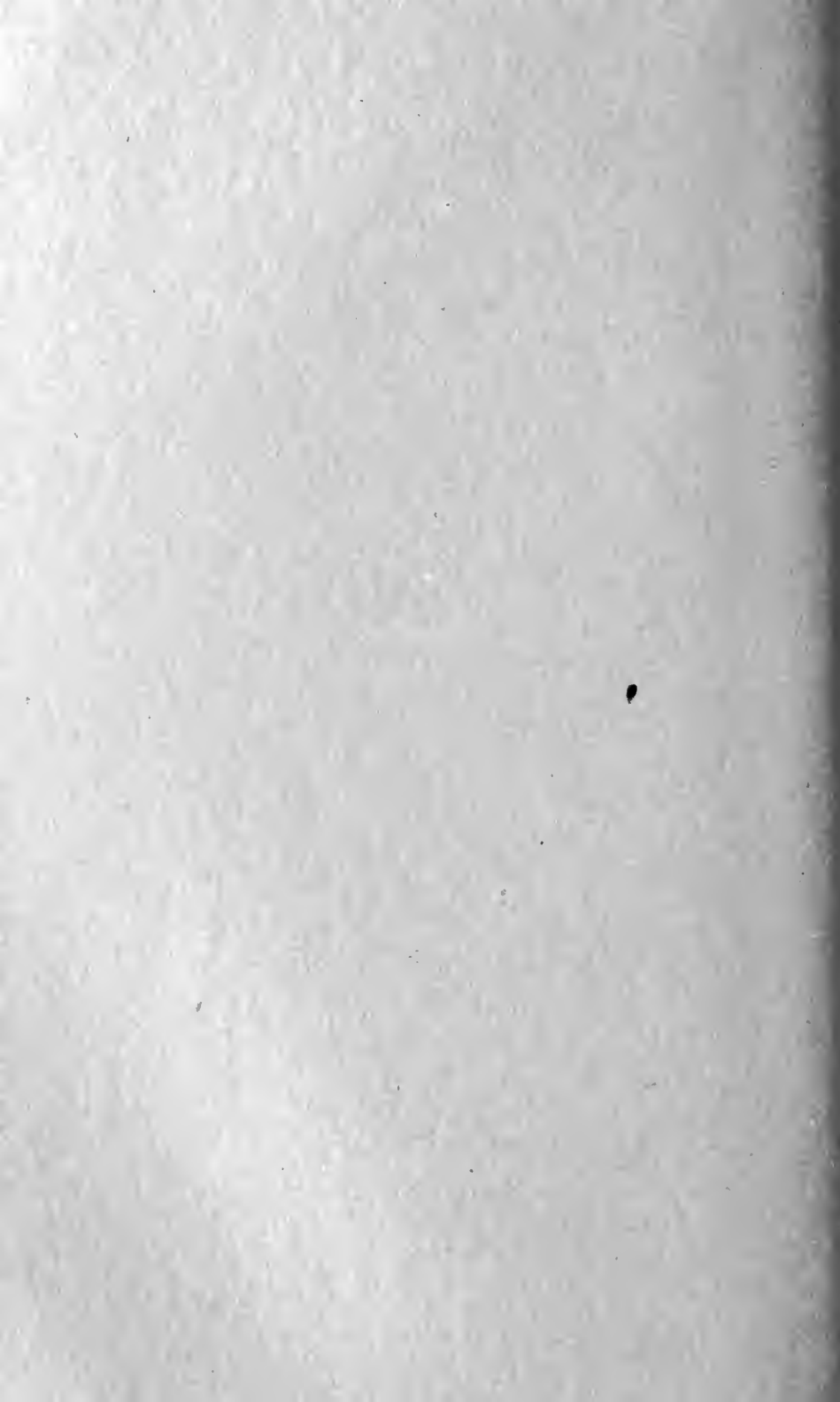
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APPELLANTS' REPLY BRIEF.

I.

Introduction.

Not only does the Government's brief utterly fail to answer the principal arguments of appellants' brief, but its own arguments are based on incorrect statements of the evidence and incorrect conclusions based thereon. As an illustration, on page 16 of its brief the Government states "Appellants admit that the 'Indoform' (Counts I and II) contained practically no posterior pituitary, though the label declares the presence of 3 units per cc. * * *." This is absolutely contrary to Bavouset's testimony that he made the posterior pituitary, had it assayed, and in manufacturing the Indoform put into the Indoform three units of posterior pituitary per cubic centimeter [R. 140-141].

On page 15 of its brief the Government states, "Only such highly unusual and improbable circumstances as boiling for five or six hours, * * * could have af-

fected the contents of the products.” The only evidence in the case with regard to boiling for five or six hours is the testimony of the witness Mason with respect to posterior pituitary [R. 74] which is involved only in connection with Counts I and II. This statement is absolutely untrue with regard to the other products. We find many instances of such misstatements in the Government brief but obviously we cannot call all of them to the Court’s attention. We, therefore, respectfully ask the Court to carefully weigh the statements and conclusions in the Government’s¹ brief before accepting them as true.

II.

Samples Must Reflect the Condition of the Product as of the Time Involved in the Issues (G. Br. 18-24).

In appellants’ opening brief we asserted that the Government did not prove its case beyond a reasonable doubt because not one iota of evidence was introduced to show proper handling of the goods *after*² they had been introduced by appellants into interstate commerce. We showed that such an absence of evidence is fatal to the Government, because there was nothing to establish that the goods when tested by the Government were in the same condition as when shipped by appellants.

We supported this argument with numerous authorities, all of which state that there must be evidence showing that the goods were properly handled and cared for (See Appellants’ Br. 21, *et seq.*).

In reply to our argument the Government first quotes from 32 Corpus Juris Secundum, Sec. 607, to the effect that, “It is unnecessary to show an absence of tampering

¹The appellee is herein referred to as the Government and its brief is referred to as “G. Br.”

²Italics may be considered ours throughout this brief.

on the part of every person through whose hands the article has passed; as long as the article can be identified it is immaterial in how many or in whose hands it has been.” (G. Br. 19).

Corpus Juris Secundum cites but one case in support of this proposition, which is the case of *Lestico v. Kuehner*, 283 N. W. 122, 204 Minn. 125. That action was one for personal injuries in which defendant offered a punctured tire casing in evidence. Now it is quite apparent on its face that the subject matter is so different that the rules of evidence which would apply in a case like the one on appeal would not be pertinent. However, even in *Lestico v. Kuehner*, the Court said (283 N. W. 122, at page 125):

“If changes had destroyed its identity or had made the object wholly worthless or of questionable value as evidence, an entirely different situation would have been presented.”

The statement quoted by the Government from Corpus Juris Secundum must be read in conjunction with the portions quoted by appellants on page 23 of their brief, which states that in order that an article may be introduced two things are necessary: first, it must be satisfactorily identified; and, second, it must be shown to the satisfaction of the Court that no substantial change has taken place such as would render the evidence misleading. A further condition with respect to samples is that the samples “must reflect the condition of the substance or articles as of the time involved in the issues.” (Appellants’ Br. 23).

Reading the two paragraphs quoted by appellants, and the single paragraph quoted by the Government, it is clear that although detailed evidence may not be required as to each person who handled the goods, nevertheless there must at least be some evidence as to care and handling, in order to support a conclusion that the goods when tested

by the Government were in the same condition as they were when shipped by appellants.

Government's brief then quotes (pp. 19, 20) from *United States v. S. B. Penick & Co.*, 136 F. (2d) 413, 415, which states that "there is no hard and fast rule that the prosecution must exclude all possibility that the article may have been tampered with." This may be true but, as stated in this same opinion, *there must be some testimony with respect to "the circumstances surrounding the preservation and custody of it, and the likelihood of intermeddlers tampering with it"* (Appellants' Br. 21).

The excerpt quoted by the Government from the *Penick* case, shows the type of evidence which may be accepted by the Court, namely:

- (1) "Here the samples were taken in the ordinary course of business for the very purpose of being retained as samples";
- (2) "they were put in the usual place of business where samples were kept";
- (3) "to remove them from accident or meddling and there they remained, so far as appears, undisturbed." (G. Br. 20.)

It should be noted that in the *Penick* case, the samples were taken when the purchaser *received* the shipment and were specially cared for as samples, whereas in this appeal, the goods were taken from several weeks to five months later and there is no evidence as to how they were cared for or handled.

In lieu of the evidence required by the authorities relied on, the Government asks the Court to indulge in a series of what it refers to as "inferences" that the goods were properly handled by the transportation companies, the doctors who received them, etc. Since there are no facts on which to base an inference, what the

Government asks is that the Court indulge in “speculation” and “guessing.”

The Government seeks to *reverse* the presumption of innocence and the burden of proof. The Government in effect says—it must be presumed that the goods are in the same condition when tested as when shipped, and the burden of proof is on the appellants to prove that the goods were mishandled.

The Government contends it undertook “to establish the identity of the samples *as of the time of shipment*, by *circumstantial* evidence relating to their interstate shipment, the identity of the consignees and the condition of the drugs when received by the Government chemists, together with the reasonable inferences flowing from such evidence” (G. Br. 20).

Also the Government asserts “It may reasonably be assumed that the doctors who received such products handled and stored them in the normal way” (G. Br. 21).

While there may be a presumption supporting the official acts of public officers, and, in the absence of evidence to the contrary, courts presume that they have properly discharged their official duties, there is *no presumption whatever* with respect to either:

- (1) That shippers and others properly handle and care for goods, so that changes cannot occur in the goods while in their custody, or
- (2) That doctors, as well as nurses and others who commonly give the patients the injections on behalf of the doctor properly handle and care for goods so that changes cannot occur in the goods after they are received by the doctor.

Furthermore, in the absence of even a single line of testimony to which the products were subjected to from the time of shipment to the time when they were picked up by the inspectors, no inference whatever can be drawn

with respect to the conditions to which the products had been subjected during shipments or while in the doctors' offices. There must be facts from which to draw an inference. Here there are none.

The Government has stipulated that doctors "deliberately insert other things into bottles to make a different combination of a product" [R. 168] and the unrebutted testimony shows that the contents of the bottles may become contaminated by materials carried by the hypodermic needle inserted through the rubber corks of the bottles [R. 161-165], therefore there is no basis whatsoever on which the Government can ask the Court to "assume" or "infer" that these things have not occurred to the products in suit while they were in the doctors' offices.

The Government further contends (G. Br. 20) that its evidence was strengthened by alleged admissions in Bavouset's testimony:

- (1) "that the product 'Indoform' was adulterated and misbranded when it was introduced into interstate commerce," and
- (2) "that all of the products here involved were likely to have been adulterated and misbranded at that time by reason of *the poor manufacturing controls maintained by the appellants.*"

As to the alleged admission with regard to Indoform, here is Bavouset's testimony:

"Q. And that is with reference to the product which became the subject matter of Counts I and II, the Indoform, and that you stated that you had had that solution *later* tested by the Cooper Laboratories who found it contained such small quantities of posterior pituitary as to be immeasurable? A. That is right; I did that.

Q. And that is, of course, *after you had shipped the product?* A. That is right." [R. 143, 144.]

Bavouset thus stated that the "product which became the subject matter of Counts I and II," namely, the contents of Ex. 3, was *later* tested by the Cooper Laboratories, *after* it had been shipped in interstate commerce. Thus it appears that Bavouset recovered some of this product after it had been shipped. How long after the evidence does not show. Nor does the evidence show how the product was handled after shipment and before it was recovered by Bavouset. There is no testimony to show that the change in the product tested by Cooper did not occur after it had been introduced into interstate commerce by appellants.

When the Government contends that the testimony referred to above is an admission of Bavouset that Indoform was not up to standard when it was introduced into interstate commerce we respectfully submit that such is a gross misinterpretation of the evidence. If the quoted testimony were construed as the Government has done, then it is contrary to Bavouset's other testimony, as to assaying the posterior pituitary and making the Indoform which will be referred to shortly. The alleged admission therefore merely goes to the credibility of the witness (See Jones on "Evidence," 4th Edition, page 557).

Jones on page 554 says, "It is a familiar rule that verbal admissions should be received with caution and subjected to careful scrutiny, no class of evidence being more subject to error or abuse." As to whether or not there was the labeled amount of posterior pituitary in Indoform we think that the best evidence is the testimony of Bavouset who testified that he made the posterior pituitary [R. 140] and knows it was up to standard because it was assayed [R. 141]. Bavouset personally

compounded the Indoform and personally measured the amount of posterior pituitary which was three International Units for each cubic centimeter of Indoform [R. 110]. No evidence could be clearer and more convincing.

As to the second alleged admission with regard to poor manufacturing controls, there is no evidence of poor manufacturing controls; but even though there were such evidence in the case this is not proof or even the basis for a presumption or inference that the goods when shipped were adulterated and misbranded.

When the Government uses the term "poor manufacturing controls" it undoubtedly refers to the fact that appellants did not always test their products at the conclusion of the manufacture. This certainly is not circumstantial evidence which would logically lead to the conclusion that the goods when shipped did not have the labeled potencies.

The corporate appellant Pasadena Research Laboratories, Inc. has been in business for six years and the appellant Bavouset has been manufacturing these preparations for twenty consecutive years [R. 108]. Bavouset has been manufacturing B-1 and B-Complex solutions for ten years and Indoform for fifteen years [R. 109]. This was the first alleged offense of either of the appellants.

Government inspectors visited the plant at Pasadena Research Laboratories very shortly after they started in business. Once a year they go through the plant very thoroughly and sometimes visit the plant as often as once a month or once every three months [R. 126]. The inspectors go through the corporation books and check their invoices of what has been shipped out [R. 127]. Thus it appears that over a long period of time the food and drug inspectors found nothing wrong with appellants' products. Apparently the inspectors found nothing

wrong with the manufacturing methods or controls used by appellants, for if they had it would have been the duty of these custodians of public health to recommend to and insist upon appellants changing their procedures.

We believe that the Government is unwarranted in drawing the conclusion with respect to appellants' manufacturing controls and that there is no inference here which can take the place of direct evidentiary proof that the goods were adulterated and misbranded when introduced into interstate commerce.

III.

Stability of Thiamine Hydrochloride in Pluri-B (Counts III and IV) and Stability of Riboflavin in Pluri-B (Count VII) (G. Br. 4, 9, 11, 15, 22, 34).

The Government's contention that "it was indisputably established that these products are extremely stable except under such unusual circumstances as boiling for five or six hours, freezing temperatures, addition of extraneous materials to contents, etc." and the many similar statements in its brief (G. Br. 22) are not in accord with the evidence.

The only testimony whatever with respect to the stability of any product whatever after being boiled for five or six hours is in connection with the stability of posterior pituitary (Count I). There is no such testimony whatever with respect to the stability of either thiamine hydrochloride (Counts III and IV) or riboflavin (Count VII) under any such conditions of temperature as "boiling for five or six hours."

The "Stability of Appellants' Products Under Heat," etc. is stated on pages 15 and 16 of Appellants' Brief and the stability of said products as affected by "Addition of Other Things Into Products" is covered on pages 16-21 of said brief.

Briefly, Dr. Icke's testimony is that thiamine hydrochloride is not stable at temperatures above 100 to 120 degrees Fahrenheit and that if the bottle, Ex. 6, "had been setting in the sunlight so that the temperature got up that high, or any other factor which might have elevated the temperature, it might have deteriorated" [R. 185].

This product, Ex. 6, was shipped from Pasadena, California, on July 16, 1945, to Reno, Nevada, was picked up by the Government inspector on August 30, 1945, and was sent to Washington, D. C. In other words, the product was shipped and handled during the heat of the summer and may well have been exposed to temperatures in excess of 100 degrees during both shipments and while in Reno.

The Government witness Capps' testimony on pages 100 and 101 of the Record is in accord with the above. He testified that thiamine hydrochloride is stable except when exposed to "extreme high temperatures," and that "heats any more than would be normal from shipping and the weather" would be excessive.

With respect to the effect of temperature on the stability of riboflavin in Pluri-B, the testimony, briefly, is that the precipitate might be due to temperature slightly above freezing [Wiley, R. 42] or to varying conditions of temperature [Bavouset, R. 145].

IV.

Reply to Government's Contention Re: Posterior Pituitary in Indoform (Counts I and II) (G. Br. 2-6, 24).

The Government argues that the posterior pituitary was below standard when the Indoform was introduced into interstate commerce and bases its argument principally on:

(1) That the tests made by Mason are reliable tests which establish that the posterior pituitary was below the labeled amount (G. Br. 4-5).

(2) That Bavouset admitted the lack of posterior pituitary (G. Br. 3).

As to the first point, we respectfully submit that Mason's own testimony clearly and convincingly establishes that he did not make a test which was capable of determining the amount of posterior pituitary present.

When asked by the Court how he could know whether posterior pituitary was present, and, if so, in what amount. Mason said "the only way that could be determined is by an assay for the presence of posterior pituitary" [R. 224]. The Court then said "It could not be determined by the test you made," and Mason answered, "that test I made is not what one might call an assay, because it is impossible to get an assay with the product under investigation" [R. 224].

We respectfully submit that this one bit of testimony alone is all that is needed to establish that Mason's test did not determine how much posterior pituitary was in the Indoform which he tested.

With respect to the alleged admission by Bavouset that the Indoform did not contain the labeled amount of posterior pituitary when shipped, we have already shown that there is no such admission in the record (see p. 6 of this brief).

The Government did not introduce any evidence tending to disprove the matters set forth on pages 16-21 of Appellants' Brief in the section entitled "Addition of Other Things Into Products," briefly

- (1) that doctors insert needles into the caps of these bottles for the purpose of withdrawing the solution from them (Appellants' Brief 16),
- (2) that doctors deliberately insert other things into bottles to make a different combination of a product (Appellants' Brief 18), and
- (3) that you can't tell whether or not a cap has been punctured by looking at it with the naked eye (Appellants' Brief 19).

Therefore, even though we assumed for the purpose of argument (and contrary to Mason's admission that he did not assay for posterior pituitary), that Mason did determine that the posterior pituitary was below standard, still the Government cannot prevail because the Government introduced no evidence to show that any one of the above things did not happen, or to show how the goods were handled after they were introduced into interstate commerce by appellants.

V.

Reply to Government's Contentions Re: Alleged Admissions and Independent Proof of Violations Re: Thyroid Substance (Counts I and II) (G. Br. 25-28).

The label, Ex. 4, states that each cubic centimeter contains "Thyroid Substance 1 gr." and bears the notation "This preparation does not contain any known therapeutically useful constituent" [R. 63].

The Government (G. Br. 16) contends that this label is misleading (1) because other constituents admittedly do have therapeutic value, and (2) there is no clear cut

statement that this particular thyroid substance does not contain the iodine constituent.

There is no merit to the Government's contention that the label is misleading because other constituents in the product do have therapeutic value. Bavouset put the disclaimer on the product after "taking into consideration the rules and regulations." His testimony is that in this particular solution, the therapeutic value of the products in the solution, "would not be measurable" [R. 135].

The second contention, namely, there is no clear cut statement that this particular thyroid substance does not contain the iodine constituent, is an admission in itself that it contains a statement to that effect.

For the reasons stated on pages 39-45 of Appellants' Brief, we submit that there is no merit to the Government's contention. Briefly, we submit that each of the following facts clearly establishes that the Government failed to prove its case:

(1) The term "thyroid substance" has acquired a very definite and distinct meaning.

There are many preparations on the market that have labels which specify "thyroid substance" that do not contain any iodine, which preparations are used daily [R. 113]. Bavouset testified that he had some of those preparations [R. 113] and the Government did not make an issue as to said products [R. 114].

Furthermore, the product is sold only to doctors who request it [R. 111], and Bavouset has been making this product over a period of about *fifteen years* [R. 109].

(2) There is no evidence with regard to any one being misled by the term "thyroid substance,"—although Bavouset has been making the product for fifteen years. The evidence is all to the contrary.

(3) The Government witness Buell's testimony is that the solution contained in the bottle, Ex. 3, was not different from anything which the label, Ex. 4, represented it to possess. His testimony is that he did draw the conclusion that there was no active substance of thyroid in that solution [R. 94, 95].

(4) Dr. Icke's testimony that any doctor looking at the label would "certainly not" expect to find thyroxin (iodine) in the solution, and that if the doctor wanted thyroid activity he would give thyroid orally [R. 177, 178].

In support of its contention the Government cites the case of *H. N. Heusner & Son v. Federal Trade Commission*, 106 F. (2d) 596.

The facts in that case are entirely different from the facts in this case. In that case the so-called "Havana Smokers" were not made in Havana, whereas in this case. the product did contain the labeled amount of "thyroid substance."

The decision in that case reads in part as follows (pages 597, 598):

"Second, it is possible, although the point is not reflected in the findings of the Commission, that the long misuse of the word 'Havana' has lent that term a species of secondary meaning in connection with petitioner's cigars. * * * Courts of equity now tend to take this fact into account before applying the doctrine of unclean hands in the manner above referred to. As a leading text writer has put it: 'They are now chiefly concerned with whether in the case of particularly well known marks and names, the public has become accustomed to associate a product with a definite taste, appearance, smell, etc. without in the least being deceived by a product which does not contain exactly what it professes to, but which is the identical article which had previ-

ously satisfied them.’ Derenberg, Trade-Mark Protection and Unfair Trading, p. 670.”

In view of the above, the Court allowed the manufacturer two years in which to eliminate the word “Havana” in designating its product, whereas in this case, although appellants and others have been selling many preparations which specify or are labeled “thyroid substance” for at least fifteen years, and such preparations are in daily use, the corporate appellant was fined the maximum of One Thousand (\$1,000.00) Dollars and the individual appellant was placed on probation for five years.

VI.

Reply to Government’s Contention Re: Alleged Admissions and Independent Proof of Violations Re: Thiamine Hydrochloride (Counts III and IV) (G. Br. 28-30).

On page 28 of its brief, the Government states, “With respect to the interstate shipment of ‘Pluri-B’ (Counts III and IV), the uncontradicted evidence is that the sample analyzed by Government witness Capps [Govt. Ex. 6] contained only 33 milligrams of thiamine hydrochloride per cc. [R. 100], though the label declares the presence of 50 milligrams of thiamine hydrochloride per cc. [R. 107].”

This statement is both false and misleading in that it implies that the evidence is uncontradicted that this product only contained 33 milligrams of thiamine hydrochloride on July 16, 1945, when the product was introduced into interstate commerce. The contrary is established on pages 4-6 of Appellants’ Brief.

Briefly, the only evidence supporting the Government’s contention is the unfounded opinion of the Government

witness Capps in response to an improper hypothetical question containing facts not proved. Please see Appellants' Brief, pages 26-32.

The testimony with respect to the stability of thiamine hydrochloride is set forth in a previous section entitled "III. Stability of Thiamine Hydrochloride in Pluri-B."

On page 29 of its brief, the Government contends that its affirmative evidence is strengthened by the admission that "defendants did not have the equipment necessary to make the thiochrome determination for thiamine." The Government again would reverse the presumption of innocence and shift the burden of proof to appellants, which is not in accordance with the law. See also page 8, *supra*.

Furthermore, the Government's contention is fully disproved by the positive testimony of Bavouset that he probably made the product [R. 114]; that at the time it was bottled it had the full strength that is set forth on the label [R. 115]; and that it had a five per cent override of thiamine hydrochloride [R. 116].

VII.

Reply to Government's Contention Re: Alleged Admissions and Independent Violations Re: Asserted Undissolved Materials in Ex. 1 (Count VII) (G. Br. 30-32).

The Government's statement "With respect to the other shipment of 'Pluri-B' (Count VII), the uncontradicted evidence is that all the vials in the sample examined by Government witness Wiley [Govt. Ex. 1] were badly contaminated with undissolved material visible to the naked eye [R. 34]." (G. Br. 30) and similar statements in its brief are false and misleading in that they imply that the evidence is uncontradicted that the product was contaminated when it was introduced into interstate commerce on June 18, 1946.

The only testimony whatever in support of that contention is the Government witness Wiley's answer in response to an improper hypothetical question which was duly objected to [R. 42].

We respectfully submit that Wiley's answer to the improper hypothetical question is not entitled to any weight whatever for the following reasons:

- (1) Dr. Wiley did not test the precipitate in Ex. 1 chemically [R. 42] and so obviously he could not tell whether the precipitate was thiamine hydrochloride, riboflavin, one of the other materials in the product, something that had been added to the solution, or a reaction product.
- (2) The hypothetical question was bad and improper in that it did not contain sufficient facts to afford grounds for a reasonable opinion or conclusion in that no mention whatever was made in it with respect to the temperature, temperature fluctuations, the addition of foreign materials, if any, or any other condition whatever to which the product had been subjected.

This contention is dealt with on pp. 26-32 of Appellants' Brief.

- (3) That Wiley testified that the product Ex. 1 contained 20 times the amount of riboflavin that would stay in solution. His testimony is that it is "20 times over-saturation" [R. 46].

Wiley failed to take into consideration the presence of nicotinamide which, as Bavouset testified, is a very fine solvent for riboflavin [R. 144, 145]. Dr. Icke's testimony on p. 170 of the Record is to the same effect.

That Wiley's statement is clearly in error is also shown by the fact that according to Wiley, Pluri-B, Ex. 6, contains 10 times the amount of

riboflavin that would stay in solution. In other words, Ex. 6, according to Wiley is "10 times over-saturation"—yet it contains no precipitate whatever.

Wiley's unfounded and worthless opinion evidence is fully disproved by the positive testimony of Bavouset and Mrs. Smiley.

Bavouset testified that the precipitate was not in these bottles when they were shipped to Dr. Ryerson on June 18, 1946, that they keep control batches for a short time after the material is shipped, and that a very careful inspection is made the last thing before the product is sent out [R. 118, 119].

Mrs. Smiley, in charge of the shipping department, testified that there were no foreign particles in these bottles when she examined them for that purpose by means of an inspection lamp [R. 121, 123].

VIII.

Reply to Government's Contention "No Error Was Committed by the District Court in Permitting the Government's Witnesses to Answer Hypothetical Questions" (G. Br. 33-39).

The Government contends that "in a criminal case which is tried by the Court without a jury it is assumed that the trial court considered only competent and material evidence; consequently, the reception of incompetent evidence is not prejudicial" (G. Br. 33). Although such may be the assumption in an ordinary case, this presumption must yield to a showing to the contrary. *Fotie v. United States*, 137 F. (2d) 831, C. C. A. 8.

In the present case the appellants were seriously prejudiced by the admission of this evidence for the reason that the District Court must have relied on the answers

to these hypothetical questions. Subtract from the evidence these improper hypothetical questions and the unfounded opinion answers given in response to them and there is absolutely no evidence of guilt whatsoever; and there is no evidence whatsoever that the products were adulterated and misbranded when introduced into interstate commerce.

In *Daniel v. United States*, 127 F. (2d) 1, C. C. A. 8, the Court pointed out that since no jury was present at the trial the reception of incompetent evidence would not be prejudicial, but stated, "the only concern of this Court (the Circuit Court) is whether the judgment is supported by some competent evidence." For the reasons set forth on pages 26 to 32 of Appellants' Brief, we respectfully submit that the hypothetical questions were bad and improper and that without the incompetent answers to these questions there is no evidence whatsoever to support the judgment finding appellants guilty of the crimes charged.

Opinion Evidence Upon the Very Question in Issue.

We fail to understand how the Government can contend that "no expert witness testified in his opinion * * * that its purity and quality fell below that which it purported and was represented to possess" (G. Br. 37).

In this connection, please compare the following:

Counts I-II [R. 2-5] with the testimony of Mason [R. 75, 76]; testimony of Buell [R. 90].

Counts III-IV [R. 5-8] with the testimony of Capps [R. 100, 101].

Count VII [R. 10-12] with the testimony of Wiley [R. 40].

All of the cases cited by the Government on pages 37, 38 and 39 of its brief are either before *United States v. Spaulding*, 293 U. S. 498, or are not in point. As the

Supreme Court held in this case, the ultimate issues should not be resolved by opinion evidence (pp. 506, 507).

This rule is not limited to war risk insurance cases and has been applied in criminal cases. *People v. Crossan*, 87 Cal. App. 5, 16, 261 Pac. 531, 536.

For example, see 32 Corpus Juris Secundum, Section 446, page 74 (citing many types of cases):

“An inference, opinion, or conclusion of a witness which is determinative of vital issues or of the ultimate fact in issue ordinarily is excluded as an invasion of the province of the jury. * * *”

See also Jones “The Law of Evidence in Civil Cases,” Section 374, pages 698 and 699.

The District Judge held in accordance with the rule at one time, but later overruled the appellants’ objection [R. 74, 75].

Conclusion.

The judgment of conviction appealed from should be reversed and the case remanded to the District Court with instructions to acquit the appellants.

Respectfully submitted,

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Los Angeles, California,
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